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IN THE

Supreme Court of the United States

RICHARD A. FREDERICK, RANDOLPH W. LENZ, KARIN LENZ and KCS INDUSTRIES, INC.,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

KEITH D. KRAKAUR
Counsel of Record
DAVID M. ZORNOW
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
Attorneys for Petitioners
Randolph W. Lenz,
Karin Lenz and KCS Industries, Inc.
919 Third Avenue
New York, NY 10022
(212) 735-3000

ANDREW J. LEVANDER
GUY PETRILLO
SWIDLER BERLIN SHEREFF
FRIEDMAN, LLP
Attorneys for Petitioner
Richard A. Frederick
919 Third Avenue
New York, NY 10022
(212) 758-9500

155668

Counsel Press LLC
FORMERLY LUTZ APPELLATE SERVICES
(800) 274-3321 • (800) 359-6859

QUESTIONS PRESENTED

1. Should this Court resolve the conflict among the Circuits as to whether a "dual-purpose" document — a document prepared for use in preparing tax returns *and* for use in litigation — can ever be subject to the attorney-client or attorney work product privileges?

2. Should this Court reverse the Seventh Circuit's holding that the attorney-client and attorney work product privileges cannot apply to an attorney's activities in the context of an IRS audit unless the attorney is performing case law and statutory analysis?

3. Should this Court reverse the Seventh Circuit's decision to apply the clearly erroneous standard of review to a mixed question of law and fact in the context of privilege determinations?

STATEMENT PURSUANT TO RULE 29.6

Petitioner KCS Industries, Inc. has no parent corporation, and no publicly held company owns 10% or more of its stock.

TABLE OF CONTENTS

	Page
Questions Presented	i
Statement Pursuant to Rule 29.6	ii
Table of Authorities	v
Table of Appendices	x
Opinions Below	1
Jurisdiction	1
Statutory Provisions Involved	1
Statement	1
Reasons for Granting the Writ	7
1. This Court Should Resolve The Conflict Among the Circuits As To Whether A "Dual-Purpose" Document — A Document Created For Use In Preparing Tax Returns *And* For Use In Litigation — Can Ever Be Subject To The Attorney-Client Or Work Product Privileges.	8
2. This Court Should Reverse The Seventh Circuit's Holding That The Attorney-Client And Work Product Privileges Cannot Apply To An Attorney's Activities In Full In The	

Contents

Page

Context Of An IRS Audit Unless The Attorney Is Performing Case Law And Statutory Analysis. 15

A. The Nature of the Audit Process Often Causes the Parties to Anticipate Litigation. 15

B. The Attorney-Client Privilege Applies to a Broad Category of Attorneys' Audit-Related Activities. 18

3. It Was Error For The Seventh Circuit To Hold That The Clearly Erroneous Standard Of Review Applies To Appellate Review Of Mixed Questions Of Law And Fact. 20

Conclusion 23

TABLE OF CITED AUTHORITIES

Page

Cases:

Badaracco v. Commissioner, 464 U.S. 386 (1984) 16

Colton v. United States, 306 F.2d 633 (2nd Cir. 1962), *cert. denied*, 371 U.S. 951 (1963) 10

Couch v. United States, 409 U.S. 322 (1973) 9

Lenz v. Commissioner, 101 T.C. 260 (1993) 17

Miller v. Fenton, 474 U.S. 104 (1985) 21

Ornelas v. United States, 517 U.S. 690 (1996) 6, 8, 20, 21, 22

Pullman-Standard v. Swint, 456 U.S. 273 (1982) .. 20

Salve Regina College v. Russell, 499 U.S. 225 (1991) 21, 22

Schuneman v. United States, 783 F.2d 694 (7th Cir. 1986) 22

Tax Analysts v. IRS, 117 F.3d 607 (D.C. Cir. 1997) 16

Trammel v. United States, 445 U.S. 40 (1980) 13

Cited Authorities

Page

United States v. Abrahams, 905 F.2d 1276 (9th Cir. 1990) 10, 22

United States v. Adlman, 134 F.3d 1194 (2nd Cir. 1998) 13, 16

United States v. Arthur Young & Co., 465 U.S. 805 (1984) 9

United States ex rel. Tonaldi v. Elrod, 716 F.2d 431 (7th Cir. 1983) 22

United States v. Kovel, 296 F.2d 918 (2d Cir. 1961) 14

United States v. Lawless, 709 F.2d 485 (7th Cir. 1983) 10

United States v. Rockwell International, 897 F.2d 1255 (3rd Cir. 1990) 9

United States v. Zolin, 809 F.2d 1411 (9th Cir. 1987), *aff'd in part and vac'd in part*, 491 U.S. 554 (1989) 22

Upjohn Co. v. United States, 449 U.S. 383 (1981) . 13, 16

Cited Authorities

Page

Statute:

28 U.S.C. § 1254(1) 1

Rule:

Fed. R. Civ. P. 26(b)(3) 15, 16

Other Authorities:

Jon Almeras, *Official Discusses Tax Shelter and Privilege Issues*, Tax Notes, May 17, 1999, available in WL, 1999 TNT 94-7 7

Peter M. Berkery, Jr., *Taxing Issues*, Accounting Today, May 10 – May 23, 1999 7

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Cited Authorities

Page

News, *TEI Asks Court to Clarify Narrow Privilege Ruling*, Tax Practice, July 12, 1999 7

Burgess J. W. Raby & William L. Raby, *Illusions, Delusions, and Tax Practice Privilege*, 83 Tax Notes 697 (1999) 7

Restatement (Third) of the Law Governing Lawyers § 122, cmt. c (Proposed Final Draft No. 1, 1996) 11, 12

Jeffrey A. Rich, *Tax Practitioner's Privilege Raises Some Thorny Issues*, 83 Tax Notes 703 (1999) . 7

Christopher S. Rizek, *When is Tax Practice 'Legal'?*, Legal Times, July 5, 1999 7

Jonathan Samel, *Attorney-Client Privilege May Not Apply When Attorneys Prepare Tax Returns*, The Legal Intelligencer, June 1, 1999 7

Seventh Circuit Applies 'Light Touch' to Privilege Claims, Federal Discovery News, June 1999 ... 7

Sheryl Stratton, *Appellate Court, in Dictum, Narrows New Tax Adviser Privilege*, 83 Tax Notes 460 (1999) 7

Sheryl Stratton, *Decision Narrowing Privilege Amended to Address Audits*, 83 Tax Notes 1110 (1999) 7

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Page

Summary, *Lawyer-Accountant Cannot Protect Summoned Papers Under Privilege*, 83 Tax Notes 516 (1999) 7

Tax Court News, *Tax Documents Made by Accountant-Lawyer Are Not Shielded by Privilege*, Business Tax News Digest, July 1999 7

Tax Preparation Documents Not Protected by Attorney-Client Privilege or Work Product Doctrine, Research Inst. of America Weekly Alert, April 29, 1999 7

TABLE OF APPENDICES

Page

Appendix A — Opinion Of The United States Court Of Appeals For The Seventh Circuit Dated, And Decided April 15, 1999, As Amended May 18, 1999 ..... 1a

Appendix B — Decision And Order Of The United States District Court For The Eastern District Of Wisconsin, Dated And Filed February 12, 1998 16a

Appendix C — Decision And Order Of The United States District Court For The Eastern District Of Wisconsin, Dated And Filed August 19, 1996 .. 29a

Appendix D — Order Of The United States Court Of Appeals For The Seventh Circuit Denying Petition For Rehearing, Dated July 26, 1999 ... 39a

Appendix E — Attachment To IRS Summons, Dated February 4, 1993 ..... 41a

Appendix F — Attachment To IRS Summons, Dated June 21, 1994 ..... 42a

Appendix G — Affidavit Of Richard A. Frederick, Dated May 26, 1995 ..... 43a

Appendix H — First Supplemental Affidavit Of Richard A. Frederick Dated June 21, 1995, With Attachment A 54a

Appendix I — Declaration Of IRS Special Agent James A. Hill, Dated October 20, 1994 ..... 59a

Richard A. Frederick, Randolph W. Lenz, Karin Lenz, and KCS Industries, Inc. (together, "Petitioners"), respectfully petition for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 182 F.3d 496 (7th Cir. 1999) (App. 1a-15a).[1]

The relevant opinions of the district court are unreported. (App. 16a-28a, 29a-38a).

JURISDICTION

The Court of Appeals entered its judgment on May 18, 1999. A petition for rehearing was denied on July 26, 1999. (App. 39a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

None.

STATEMENT

The Internal Revenue Service ("IRS") has been litigating against Petitioner Randolph W. Lenz and companies under his control for more than ten years. As set forth more fully below, Petitioners, in connection with the IRS's investigation of the personal returns of Randolph W. and Karin Lenz for the tax years 1988 through 1992, have invoked the

1. "App." refers to the Appendix filed herewith.

protections of the attorney-client privilege and the attorney work product doctrine to shield from production to the government in a tax summons enforcement proceeding confidential workpapers and written communications and memoranda prepared by the Lenzes' tax attorney, Petitioner Richard A. Frederick.

This petition seeks review of the Seventh Circuit Court of Appeals' rulings that as a matter of law: (a) a confidential document prepared by an attorney functioning both as tax law counsel and as a tax return preparer cannot enjoy the protections of the attorney-client privilege and the attorney work product doctrine; (b) the privileges are inapplicable in the context of an IRS audit, except as to case law and statutory analysis by the taxpayer's attorney, even where litigation is anticipated; and (c) a clear error, rather than *de novo*, standard of review applies to appellate review of privilege determinations involving mixed questions of law and fact.

Mr. Lenz is a businessman who has specialized in turning around financially troubled entities. He is married to Petitioner Karin Lenz. KCS Industries, Inc. ("KCS") is a management company that during the relevant period was controlled by Mr. Lenz, who served as both KCS's Chief Executive Officer and its Chairman of the Board. (App. 31a).

Beginning in the late 1970's, Mr. Frederick, an attorney specializing in tax law, began to represent the Lenzes, first in connection with an IRS audit of their personal tax returns for the years 1976 through 1979. Thereafter, over the ensuing 17 years, Mr. Frederick prepared the Lenzes' personal tax returns, advised them on tax planning matters and represented the Lenzes and entities associated with them in IRS audits.

In every year since they first engaged Mr. Frederick, the Lenzes have undergone at least one audit of their personal return or a return of one of the related business entities. Mr. Frederick also represented the Lenzes in Tax Court litigations arising from certain of the audits, including litigations pertaining to the Lenzes' personal returns for 1984, 1986, 1987 and 1988. (App. 32a).

As a consequence of this constant stream of IRS investigations and lawsuits, Mr. Frederick and his clients came to expect that every tax return they or an associated entity would file would be audited and potentially litigated. As his clients expected, Mr. Frederick therefore assessed information he received from the Lenzes and their companies both for its implications in pending audits or Tax Court litigation and also with a view toward future audits and litigation. Likewise, Mr. Frederick evaluated and advised his clients on alternative tax reporting positions with the same audit and litigation concerns in mind. (App. 46a, 49a-50a).

In connection with its serial investigations of the Lenzes, the IRS issued a summons dated February 4, 1993, to Mr. Frederick for "all records . . . relating to tax work performed for Randolph W. and Karin Lenz . . . for the years 1988, 1989, 1990 and 1991." Attachment to February 4, 1993 Summons. (App. 41a). Referring to an audit of the Lenzes and KCS that had already taken place, this summons also demanded records "furnished by" the Lenzes and KCS "for the purposes of responding to the Internal Revenue Service income tax audit . . . for the years 1988 and 1989." Later, the IRS issued a second summons to Mr. Frederick dated June 21, 1994, calling for "[a]ny and all records . . . relative to the financial transactions of Randolph W. Lenz" for the year 1992. Attachment to June 21, 1994 Summons.

(App. 42a). Pursuant to these summonses, Mr. Frederick provided the IRS with thousands of pages of documents, withheld certain other documents on grounds of the attorney-client privilege and the attorney work product doctrine — a group of documents that by negotiation between Mr. Frederick and the IRS was eventually narrowed to approximately 90 — and submitted to an in-person IRS interview, again preserving the privileges by refusing to answer any question that Mr. Frederick believed infringed upon privileged communications with his clients. (App. 32a-33a). The documents withheld from production or redacted included certain memoranda, draft returns (none of which was identical to a final filed return), handwritten notes and draft worksheets, correspondence and faxes.

The government commenced summons enforcement proceedings with regard to the withheld documents on November 16, 1994. On August 19, 1996, the district court issued a Decision and Order ("August 19 Order") on the government's motion for summary enforcement. (App. 29a-38a). The court ordered summary enforcement of the summonses with regard to draft documents and worksheets, except those that reflected additional communications. (App. 37a). As to the remaining documents, the district court denied the motion and directed Mr. Frederick to submit them to the court for *in camera* review. (App. 38a). On December 20, 1996, the district court issued a consent order staying enforcement of the August 19 Order indefinitely pending the court's resolution of the remaining privilege claims.

On February 12, 1998, the district court issued a second Decision and Order ("February 12 Order") upholding Petitioners' claims as to a small number of the remaining documents and denying them as to all others. (App. 16a-

28a). The district court issued its Final Order on April 28, 1998, directing Mr. Frederick to comply with the court's prior orders and denying Petitioners' motion to reconsider with respect to one document.

On September 24, 1998, the Court of Appeals for the Seventh Circuit stayed the district court's final order pending appeal.

On April 15, 1999, an appellate panel issued a decision affirming the district court's final order in full.[2] The panel *sua sponte* amended that opinion on May 18, 1999 (amended opinion) (App. 1a-15a). Petitioners sought a rehearing with a suggestion for rehearing *en banc*. The Court of Appeals denied this petition on July 26, 1999. (App. 39a-40a). Petitioners thereafter applied to this Court for a stay pending decision with respect to the instant petition. Justice Stevens denied this application on August 19, 1999.

The appellate panel, in affirming the district court, issued three holdings that are at issue in this Petition. First, in conflict with the decisions of two other Circuit Courts, the panel ruled that documents created by an attorney for two purposes — for use in litigation and for use in preparing tax returns — cannot be privileged. Here, the panel held that Mr. Frederick's clients ran the risk by using Mr. Frederick as both tax return preparer and tax attorney that Mr. Frederick's "legal cogitations borne out of his legal representation of them would creep into his worksheets and so become discoverable by the government." (App. 8a).

2. Before publication of the original opinion, the panel *sua sponte* amended the opinion, and the original opinion is not published. *See United States v. Frederick*, Nos. 98-2644, 98-2700, 1999 WL 22947 (7th Cir. Apr. 15, 1999).

Second, the panel held that in the context of audit proceedings, Petitioners could not, except in limited circumstances, avail themselves of the protections of the attorney-client privilege or the attorney work product doctrine. Acknowledging that an audit is a "possible antechamber to litigation," the panel nevertheless held that work product prepared by an attorney in an audit that does not "deal with statutory interpretation or case law that the revenue agent may have raised in connection with his examination of the taxpayer's return," is not eligible for work product protection. (App. 9a). Third, purporting to distinguish this Court's opinion in *Ornelas v. United States*, 517 U.S. 690, 696-97 (1996), the panel majority held that because the case did not present constitutional questions, a "clear error" standard of review was appropriately applied to the mixed questions of law and fact inherent in the district court's privilege determinations. (App. 2a-4a). In a concurring opinion that otherwise agreed with the majority's analysis and decision, Judge Diane P. Wood disagreed with the majority's holding that a "single standard of review 'generally' applies to mixed questions, or that there is some kind of 'presumption' in non-constitutional cases," (App. 14a) (Wood, J., concurring), and expressed the view that an appellate court, consistent with *Ornelas*, should determine the applicable standard of review only after examining the nature of the issues presented and determining whether "searching appellate review would clarify legal doctrine." Here, Judge Wood agreed with the panel majority that a clear error standard of review was appropriate in the review of privilege determinations based on the *Ornelas* factors. *Id.*

REASONS FOR GRANTING THE WRIT

In a decision that has engendered substantial critical commentary,[3] the Court of Appeals effectively held that, regardless of the intentions of client and attorney in creating a document, whenever a tax attorney assumes the dual role of attorney and tax-return preparer, no document authored

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3. *See, e.g.*, Steven M. Harris, Letter to the Editor, *Another Nominee for Worst Tax Decision of the Year*, 83 Tax Notes 1812 (1999); Jon Almeras, *Official Discusses Tax Shelter and Privilege Issues*, Tax Notes, May 17, 1999, available in WL, 1999 TNT 94-7; Peter M. Berkery, Jr., *Taxing Issues*, Accounting Today, May 10 – May 23, 1999; Michael M. Conway & Jonathan P. Biller, *The Seventh Circuit Delivers Blow to Evidentiary Privileges in Tax Matters*, Executive Briefing (June 30, 1999); Molly McDonough, *Privilege Ruling Worries Tax Lawyer/Accountants*, Chicago Daily Law Bulletin, May 27, 1999; Burgess J. W. Raby & William L. Raby, *Illusions, Delusions, and Tax Practice Privilege*, 83 Tax Notes 697 (1999); Jeffrey A. Rich, *Tax Practitioner's Privilege Raises Some Thorny Issues*, 83 Tax Notes 703 (1999); Christopher S. Rizek, *When is Tax Practice 'Legal'?*, Legal Times, July 5, 1999, at S24; Jonathan Samel, *Attorney-Client Privilege May Not Apply When Attorneys Prepare Tax Returns*, The Legal Intelligencer, June 1, 1999; Sheryl Stratton, *Appellate Court, in Dictum, Narrows New Tax Adviser Privilege*, 83 Tax Notes 460 (1999); Sheryl Stratton, *Decision Narrowing Privilege Amended to Address Audits*, 83 Tax Notes 1110 (1999); Summary, *Lawyer-Accountant Cannot Protect Summoned Papers Under Privilege*, 83 Tax Notes 516 (1999); *Seventh Circuit Applies 'Light Touch' to Privilege Claims*, Federal Discovery News, June 1999; Tax Court News, *Tax Documents Made by Accountant-Lawyer Are Not Shielded by Privilege*, Business Tax News Digest, July 1999; *Tax Preparation Documents Not Protected by Attorney-Client Privilege or Work Product Doctrine*, Research Inst. of America Weekly Alert, April 29, 1999, at 199; News, *TEI Asks Court to Clarify Narrow Privilege Ruling*, Tax Practice, July 12, 1999.

by that attorney can be privileged if the document relates both to tax law analysis *and* tax return preparation. The Court of Appeals' decision also effectively ruled that the attorney-client privilege and work product doctrine are narrowly limited where an attorney represents a client in a tax audit. Together, these rulings threaten virtually to extinguish the attorney-client and work product privileges in the tax law context. Particularly here, where the tax issues in question were the subject of contemporaneous tax litigation and, for part of the relevant period, a criminal tax investigation by the IRS, this result is error and should be reversed.

Moreover, the Supreme Court's review of this mattter is well warranted because the Seventh Circuit's rulings are in conflict with decisions of two other United States Courts of Appeals, and because the panel majority's determination of the appropriate standard of review in this case was erroneous under *Ornelas*, *supra*.

1. This Court Should Resolve The Conflict Among The Circuits As To Whether A "Dual-Purpose" Document — A Document Created For Use In Preparing Tax Returns *And* For Use In Litigation — Can Ever Be Subject To The Attorney-Client Or Work Product Privileges.

The Court of Appeals' opinion holds that no document relating to both an attorney's contemporaneous provision of legal services and the preparation of tax returns can be protected by the attorney-client or work product privileges. "By using Frederick as their tax preparer," the Court wrote, "the Lenzes ran the risk that his legal cogitations born out of his legal representation of them would creep into his worksheets and so become discoverable by the Government."

(App. 8a). "Put differently, a dual-purpose document — a document prepared for use in preparing tax returns *and* for use in litigation — is not privileged." *Id.* (emphasis in original). This holding should be reversed.

Most of the documents at issue in this case were prepared by or for Mr. Frederick, when he was engaged both to prepare the Lenzes' tax returns and to provide the Lenzes with tax law advice and counsel with respect to ongoing audits and anticipated investigations and litigation. Further, some of the documents were created when Mr. Frederick was providing the Lenzes with legal advice with respect to a criminal investigation that Mr. Frederick learned of in early 1993. (App. 59a-60a). The Court of Appeals, however, declined to consider whether the documents reflected privileged communications or work product, ruling that the mere fact that the documents were also related to tax return preparation negated any privilege.

In so ruling, the Court of Appeals relied on *United States v. Arthur Young & Co.*, 465 U.S. 805, 817-19 (1984), and *Couch v. United States*, 409 U.S. 322, 335 (1973), for the proposition that an attorney's documents related to tax return preparation are discoverable. (App. 4a-5a). These cases, however, have no bearing here because *no* legal advice was at issue in either *Arthur Young* or *Couch*.[4]

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4. *Arthur Young* is also inapposite because the accountants in that case did not prepare returns but reviewed a company's financial statements, as required by the federal securities laws. 465 U.S. at 808. This distinction is critical because independent auditors have a duty to the public that abrogates privilege. *See United States v. Rockwell International*, 897 F.2d 1255, 1265 n.6 (3rd Cir. 1990) (distinguishing *Arthur Young*).

Moreover, other circuit courts have ruled that communications in furtherance of such services are subject to the attorney-client privilege. *See United States v. Abrahams*, 905 F.2d 1276, 1284 (9th Cir. 1990) ("Although communications made solely for tax return preparation are not privileged, communications made to acquire legal advice about what to claim on tax returns may be privileged."); *Colton v. United States*, 306 F.2d 633, 637 (2nd Cir. 1962) ("There can, of course, be no question that the giving of tax advice and the preparation of tax returns . . . are basically matters sufficiently within the professional competence of an attorney to make them prima facie subject to the attorney-client privilege."), *cert. denied*, 371 U.S. 951 (1963). Left undisturbed, the Court of Appeals' decision would result in differing rules of privilege for taxpayers in the Seventh Circuit, on the one hand, and the Second and Ninth Circuits, on the other. Such a split in rules is destructive of an equitable and unified national system of taxation in which taxpayers are treated by one set of rules and procedures.

While the privileges obviously do not attach to the "scrivener" work of putting appropriate numbers on a tax return, *e.g.*, *United States v. Lawless*, 709 F.2d 485 (7th Cir. 1983),[5] not all documents that an attorney reviews or creates in the course of tax return preparation necessarily fall into such category or are intended ultimately to be disclosed. Certain of an attorney's analyses that may be incident to final return preparation — such as determining what the law says about a particular tax issue, applying that law to the taxpayer's facts, and then making a judgment about what the appropriate course of action should be in light of the

5. Indeed, Mr. Frederick produced to the IRS thousands of pages of documents, many of which fall into this category. (App. 32a).

potential for audit and litigation — are classic examples of privileged and confidential legal services. Likewise, where an attorney is asked to opine on the tax consequences of a proposed transaction, there may well be several ways in which the transaction can be structured, each resulting in a different tax consequence. There may also be several ways in which the completed transaction may be reported on the taxpayer's return. The attorney may give advice on how the law would apply under different factual assumptions and may illustrate such advice with numerical calculations.

Mr. Frederick represented in the district court that the documents at issue reflect both his legal analysis and his communications with the Lenzes concerning the legal questions he reviewed. *See* Sealed Appendix ("Sealed App.") submitted with Affidavit of Richard A. Frederick in Opposition to Government's Motion to Summarily Enforce Two IRS Summonses, at 2-12.[6] Pursuant to his clients' instruction, Mr. Frederick did more than simply organize and transmit information to the IRS. The documents in question, including the correspondence, worksheets, and draft returns, were intended, *inter alia*, to facilitate discussion about the Lenzes' reporting choices and how to structure their activities and the ownership of their assets to minimize the likelihood of an IRS challenge. The documents do not simply reflect the underlying detail supporting the information set forth on the filed returns.[7]

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6. This sealed document is on file with the district court.

7. The draft Restatement of the Law Governing Lawyers recognizes the distinction between unprotected scrivener's work and protected legal analysis. Restatement (Third) of the Law Governing Lawyers § 122, cmt. c (Proposed Final Draft No. 1, 1996). The Restatement contrasts two situations. Where the client's tax returns

(Cont'd)

Furthermore, the Court of Appeals' reasoning assumes, incorrectly, that the tax attorney performs no service different from that provided by an accountant. To the extent that the attorney provides legal advice, such advice falls outside the scope of the accountant's proper role. The Court of Appeals ignores this distinction by creating a one-size-fits-all "dual-purpose" rule that sweeps the two categories of professional activity together and does not inquire into the nature of the services motivating the creation of particular documents. Notably, for example, the Court of Appeals drew no distinction between information that is exchanged confidentially between client and attorney that does not appear on the final return and information that does appear on the final return. Thus, under the Court of Appeals' holding, even if client and attorney intend a confidential communication between them to promote a tax law analysis by counsel concerning a reporting position that is *not* ultimately adopted and effected on the final filed return, the confidential communication would enjoy no protection. While documents reflecting information that is intended to be disclosed are plainly discoverable, documents reflecting the information and analysis that is not intended for disclosure should not be.

(Cont'd)
are simple and the client has never discussed any legal tax questions with the attorney/tax return preparer, the Restatement suggests that "[t]he trier of fact may, but need not, infer the Client's purpose was not that of obtaining legal assistance." *Id.* § 122, cmt. c, illus. 2. In the more complex case, where the lawyer "drafts documents and provides other legal assistance relating to a complicated transaction having important tax implications that Client and Lawyer identify and discuss," and the lawyer then prepares the tax returns, "[t]he circumstances indicate that Lawyer is providing legal services in preparing the tax return." *Id.* § 122, cmt. c, illus. 3.

Under the Court of Appeals' ruling, a client who hires a lawyer to provide tax law advice and prepare tax returns will find that otherwise privileged and confidential communications are now subject to disclosure. Indeed, the Court of Appeals' opinion would support enforcement of a government subpoena *ad testificandum* for an attorney's testimony as to communications with his client concerning tax law issues. Such a regime obviously risks a substantial chilling of the attorney/client relationship, contrary to the purposes of the privilege. *See Trammel v. United States*, 445 U.S. 40, 51, (1980); *Upjohn Co. v. United States*, 449 U.S. 383, 392 (1981).

The Court of Appeals for the Second Circuit, in the context of a dispute over the applicability of the attorney work product doctrine, held that a document prepared in part in anticipation of litigation *and* in part for a non-privileged purpose — to assist with a business decision — was attorney work product subject to the protection of the work product doctrine. *United States v. Adlman*, 134 F.3d 1194 (2nd Cir. 1998). The court rejected the government's argument that the business purpose behind the document negated the privilege, stating that such a position "threatens to deny protection to documents that implicate key concerns underlying the work product doctrine." *Id.* at 1199. For the same reason, in this case, the fact that a document concerned tax return preparation in some manner should not preclude analysis of whether that document is subject to the protections of the privileges. Particularly where, as here, a criminal investigation was in progress for part of the relevant period, and common tax issues pervaded the contemporaneous audits and litigation, the privileged element of Mr. Frederick's services should be preserved rather than forfeited contrary to his clients' expectations.

The work product doctrine independently protects many of the documents here. As the Court of Appeals acknowledged, "when Frederick was doing these worksheets and filling out the Lenzes' tax returns, he knew that the IRS was investigating the Lenzes and their company, albeit in connection with different tax years, and he was representing them in that investigation." (App. 7a-8a). And, as Mr. Frederick stated,

> [i]n conjunction with the preparation of their returns I would advise the Lenzes and the entities associated with them about how reporting positions taken on their returns would affect or be affected by past, current and future tax audits and tax litigation relating to the Lenzes and the entities associated with them.

(App. 49a). Moreover, many of the same issues recurred in the IRS's examinations from year to year. (App. 47a-49a). Accordingly, Mr. Frederick's anticipation of litigation was amply justified, and the work product doctrine applicable.[8]

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8. While it may be the case that client-attorney relationships can be structured to avoid the Seventh Circuit's ruling with respect to dual-purpose communications, such efforts would be costly and cumbersome. Although it is far from clear following the Court of Appeals' opinion that a client could preserve the applicable privileges notwithstanding the court's opinion by retaining one professional to prepare his return and, separately, an attorney to evaluate tax law questions (and perhaps one or more additional professionals to assist the attorney in his work, *e.g.*, *United States v. Kovel*, 296 F.2d 918 (2d Cir. 1961)), to the extent that such a structure could accomplish this goal, it would do so only at great cost to the client. A client should be able to secure the services of a single attorney/tax preparer without ceding the protections of the privileges.

2. This Court Should Reverse The Seventh Circuit's Holding That The Attorney-Client And Work Product Privileges Cannot Apply To An Attorney's Activities In Full In The Context Of An IRS Audit Unless The Attorney Is Performing Case Law And Statutory Analysis.

The Court of Appeals concluded that "[t]he most difficult question presented by this appeal . . . relates to documents . . . prepared in connection with audits of the taxpayers' returns." (App. 9a). Acknowledging the absence of precedent, the Court concluded that in the audit context, solely case law and statutory analysis by an attorney should be eligible for protection. The Seventh Circuit's ruling — which is based on an unsupported view of the scope of an attorney's role in an audit — should be overturned.

A. The Nature of the Audit Process Often Causes the Parties to Anticipate Litigation.

The Court of Appeals' refusal to apply the analysis mandated by the work product doctrine to documents prepared in connection with audits of the Lenzes' returns is error because the very nature of those documents places them squarely within the scope of the work product privilege set forth in the Federal Rules of Civil Procedure.

Federal Rule of Civil Procedure 26(b)(3) provides that otherwise discoverable documents are protected from disclosure if they are "prepared in anticipation of litigation" by a party or a party's "representative." Both prongs of this test were easily met here. First, the audit is an adversarial process between the taxpayer and the government that may create an expectation of litigation. As the Court of Appeals itself acknowledged, the audit is a "possible antechamber to

litigation". (App. 9a). Second, because the work product doctrine applies regardless of who the taxpayer's "representative" is, it is irrelevant whether that person is acting as an attorney or an accountant. Thus, Rule 26(b)(3) plainly authorizes application of the work product doctrine in the tax audit context. *See, e.g.*, *Adlman*, 134 F.3d at 1204 (doctrine applicable to a document created before the relevant transaction was effected and long before any IRS audit commenced); *see also Upjohn Co. v. United States*, 449 U.S. 383, 397 (1981) (noting the government had "wisely" conceded that the work product doctrine applies to IRS summonses). Indeed, as the Court of Appeals for the District of Columbia Circuit held in the context of a Freedom of Information Act suit, IRS field service advice memoranda to IRS General Counsel regarding "the scope, direction or emphasis of audit activity" are protected by the attorney-client privilege and the work product doctrine when prepared in anticipation of litigation. *Tax Analysts v. IRS*, 117 F.3d 607, 619-20 (D.C. Cir. 1997). The same should apply to confidential taxpayer work product.

The Court of Appeals describes the audit process as "a stage in the determination of tax liability, often leading to the submission of revised tax returns." (App. 9a). While an audit may lead to a revised tax liability, it seldom leads to revised tax returns. In any case, documents prepared in anticipation of litigation that are generated in response to audit questions should be protected regardless of the audit's outcome. Indeed, the submission of revised tax returns does not bar the possibility of future litigation.[9] Moreover, it is possible that there will be no settlement averting litigation.

9. *See, e.g.*, *Badaracco v. Commissioner*, 464 U.S. 386 (1984) (holding that the filing of amended returns is not a defense to the application of the tax fraud provisions of Internal Revenue Code when earlier-filed returns were fraudulent).

To the Lenzes, the prospect that litigation with the IRS would occur had been a virtual certainty for some time prior to the beginning of the relevant audit. They or their companies had been audited by the IRS every year since 1981, with many of the same or similar issues arising each time, and they retained Mr. Frederick precisely because they needed legal advice and representation in tax audits, investigations and Tax Court litigation, both existing and anticipated. During the time period in which the documents at issue were created (*i.e.*, 1989 through 1993), the IRS issued a statutory notice of deficiency to the Lenzes regarding the 1988 tax year (October 2, 1992); the Lenzes filed a Tax Court petition regarding the 1988 tax year (January 5, 1993), (App. 46a); the IRS audited Terex Corporation (a corporation of which Mr. Lenz was a part-owner and Chairman of the Board), an audit in which Mr. Lenz was represented by Mr. Frederick regarding the tax years 1987-1990 (App. 55a, 57a-58a); and there was a pending Tax Court litigation on behalf of the Lenzes regarding the tax years 1987-1990, in which Mr. Frederick again represented the Lenzes, *see Lenz v. Commissioner*, 101 T.C. 260 (1993). Furthermore, Mr. Frederick knew no later than February 1993 that the IRS had commenced a criminal investigation of his clients' tax reporting.[10] Given this history, Mr. Frederick reasonably anticipated that future litigation was inevitable. (App. 49a-50a). These uncontested facts amply support application of the work product doctrine to the documents in question.

Finally, the Court of Appeals' failure to apply the work product doctrine in the audit context is inconsistent with the

10. In fact, one audit-related document specifically mentioned by the Court of Appeals was created by Mr. Frederick because of a criminal investigation of the Lenzes' tax reporting. *See* App. 8a-9a; *See also* Document Inventory at 21 (on file in the district court).

Court's own description of the purposes of the doctrine, to wit, "to prevent a litigant from taking a free ride on the research and thinking of his opponent's lawyer." (App. 5a). If the IRS were permitted to discover materials prepared by a taxpayer or a taxpayer's legal representative during an audit, those materials could provide a road map for the remainder of the audit or ensuing litigation. To the extent the materials reflected the taxpayer's or lawyer's mental impressions as to the issues at hand, and of their relative strengths and weaknesses, the IRS would be taking precisely the "free ride" the work product doctrine is designed to prevent.

B. The Attorney-Client Privilege Applies to a Broad Category of Attorneys' Audit-Related Activities.

The Court of Appeals also ruled that the attorney-client privilege may attach only to a very narrow subset of audit-related work performed by an attorney:

> When a revenue agent is merely verifying the accuracy of a return, often with the assistance of the taxpayer's accountant, this is accountants' work and it remains such even if the person rendering the assistance is a lawyer rather than an accountant. Throwing the cloak of privilege over this type of audit-related work of the taxpayer's representative would create an accountant's privilege usable only by lawyers. If, however, the taxpayer is accompanied to the audit by a lawyer who is there to deal with issues of statutory interpretation or case law that the revenue agent may have raised in connection with his examination of the taxpayer's return, the

> lawyer is doing lawyer's work and the attorney-client privilege may attach.

(App. 9a). The examples of audit-related work cited by the Court fall at the extreme ends of the spectrum of legal services that may be provided in an audit. This narrow focus misguidedly excludes from the scope of the privileges a substantial range of legal services that often occur in the audit process.

For example, in representing a taxpayer during an audit, an attorney often gathers evidence to give the client legal advice. Part of that advice concerns, as it did here, how to respond to IRS requests for information and how to choose and present information. There is no question that the information, in its final responsive form, is intended to be provided to the IRS and thus is not privileged. But previous communications concerning such information, including draft responses shared between attorney and client, are often confidential and in furtherance of the development of a final document or position to be presented to the auditor. Such attorney-client communications are classic examples of privileged documentation. To the extent litigation is anticipated, such documents also generally constitute attorney work product. By too narrowly characterizing the attorney's function in a typical audit, the Court of Appeals' opinion unduly narrowed the scope of the privilege.

Further, the Court of Appeals itself acknowledged that the privilege is intended to "assist the lawyer in giving the client good advice (which may head off litigation, bring the client's conduct into conformity with law, or dispel legal concerns that are causing the client unnecessary anxiety or inhibiting him from engaging in lawful, socially productive

activity)." (App. 5a). If confidential attorney-client communications during tax audits must be disclosed, these objectives will be frustrated.

3. It Was Error For The Seventh Circuit To Hold That The Clearly Erroneous Standard Of Review Applies To Appellate Review Of Mixed Questions Of Law And Fact.

The panel majority held that as to all nonconstitutional mixed issues of law and fact, the clear error standard of review should be applied. (App. 3a-4a). This holding is unsound in light of this Court's holding in *Ornelas*, *supra*.

In the present case, the district court announced the novel rule that documents in numerical form are inherently non-privileged, accountant-type documents. In a ruling not directly addressed by the Court of Appeals, the district court stated, "*Numbers reflect information reported to an accountant but not confidential communication between a client and an attorney. Thus, these documents are not protected.*" (App. 36a) (emphasis added). The district court thus articulated a *per se* rule that numerically expressed communications from Mr. Lenz to Mr. Frederick, and Mr. Frederick's numerically expressed work product, were not privileged "attorney-type" statements. This holding has no basis in any decision cited either by the district court or the Court of Appeals.

Here, the core dispute concerns the scope of the rules of privilege, in much the same way as *Ornelas* focused on "whether the rule of law as applied to the established facts is or is not violated." 517 U.S. at 696-97 (citing *Pullman-Standard v. Swint*, 456 U.S. 273, 290 n.19 (1982)). The government and Petitioners do not disagree on "what

happened": the communications at issue are memorialized and the relevant facts in Mr. Frederick's affidavit are uncontested. The district court took no live testimony, and the panel cited no predominantly factual finding of the district court to which it was deferring. The central issue is whether the fact that a document has a dual purpose or relates to an audit out of which litigation was anticipated conclusively resolves the privilege analysis against the party asserting the privilege where that document consists principally of numerical content. The concurring opinion noted the predominance of this legal issue on appeal: "without flagging it . . . the majority has also made an important legal ruling that affected its review: dual-purpose documents are not privileged." (App. 15a) (Wood, J., concurring).

Nothing in *Ornelas*, which the panel majority distinguishes as a constitutional case, suggests that its holding is restricted solely to the constitutional realm. Rather than focusing on whether a case is constitutionally based, this Court in *Ornelas* noted that "independent review" of a mixed question is appropriate where the rule of law can "acquire content only through application" to specific facts. *Ornelas*, 517 U.S. at 697. The Court further stated that *de novo* review is appropriate where it would give the appellate court an opportunity to "unify precedent and stabilize the law." *Id.* at 698; *see also Miller v. Fenton*, 474 U.S. 104, 114 (1985) (noting that when "the relevant legal principle can be given meaning only through its application to the particular circumstances of a case," too deferential a standard of review can "strip a federal appellate court of its primary function as an expositor of law."). The Court further noted that *de novo* review of mixed questions in cases with frequently recurring fact patterns can "usefully add to the body of law on the subject," a factor favoring such independent review. *Ornelas*, 517 U.S. at 698; *cf. Salve*

Regina College v. Russell, 499 U.S. 225, 233 (1991). ("[W]e have held that deferential review of mixed questions of law and fact is warranted when it appears that the district court is better positioned than the appellate court to decide the issue in question or that probing appellate scrutiny will not contribute to the clarity of legal doctrine.") (citations omitted). Thus, whether *de novo* review is applicable does not depend on the constitutional or non-constitutional nature of the mixed question in issue. *See Frederick* (App. 13a) (Wood, J., concurring) ("the source of the law that contributes the legal components to the 'mixed' question logically has nothing to do with the depth of the appellate review").

Each of the above-mentioned policy factors militates in favor of *de novo* review in this case. And, consistent with this Court's reasoning in *Ornelas*, the Seventh Circuit has applied *de novo* review to mixed questions in non-constitutional cases. *See, e.g., Schuneman v. United States*, 783 F.2d 694, 699 (7th Cir. 1986) (stating, in case involving valuation of farmland, that "the issue is a mixed question of law and fact" and that "in this circuit such determinations are independently reviewable by an appellate court") (*citing United States ex rel. Tonaldi v. Elrod*, 716 F.2d 431, 437 (7th Cir. 1983). The Ninth Circuit, moreover, has held that review of rulings on the scope of the attorney-client privilege should be *de novo*. *See Abrahams*, 905 F.2d at 1282 (*citing United States v. Zolin*, 809 F.2d 1411, 1417 (9th Cir. 1987), *aff'd in part and vac'd in part on other grounds*, 491 U.S. 554 (1989)).

Because questions of law predominate in the mixed question at issue in this case, *de novo* review of the district court's rulings would fulfill the appellate court's role. The panel's decision should accordingly be reversed.

CONCLUSION

The Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

KEITH D. KRAKAUR
Counsel of Record
DAVID M. ZORNOW
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
Attorneys for Petitioners
Randolph W. Lenz, Karin Lenz
and KCS Industries, Inc.
919 Third Avenue
New York, NY 10022
(212) 735-3000

ANDREW J. LEVANDER
GUY PETRILLO
SWIDLER BERLIN SHEREFF
FRIEDMAN, LLP
Attorneys for Petitioner
Richard A. Frederick
919 Third Avenue
New York, NY 10022
(212) 758-9500

APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DATED AND DECIDED APRIL 15, 1999, AS AMENDED MAY 18, 1999

United States of America,

Plaintiff-Appellee,

v.

Richard A. Frederick,

Defendant-Appellant,

and

Randolph W. Lenz, Karin Lenz, and
KCS Industries, Inc.,

Intervening Defendants-Appellants.

Nos. 98-2644, 98-2700

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

* * *

January 8, 1999, Argued
April 15, 1999, Decided

As Amended May 18, 1999.

* * *

Appendix A

JUDGES: Before Posner, Chief Judge, and Kanne and Diane P. Wood, Circuit Judges.[1] Diane P. Wood, Circuit Judge, concurring.

OPINION BY: POSNER

OPINION: Posner, Chief Judge. These appeals challenge an order enforcing summonses that the Internal Revenue Service issued to Richard Frederick. Frederick is both a lawyer and an accountant, and he both provides legal representation to, and prepares the tax returns of, Randolph and Karin Lenz and their company, KCS Industries, Inc. The IRS is investigating the Lenzes and their company, and the summonses directed Frederick to hand over hundreds of documents that may be germane to the investigation. Frederick balked at handing over all of them, claiming that some were protected by either the attorney-client privilege or the work-product privilege (or both). His refusal precipitated this enforcement proceeding. 26 U.S.C. § 7604(b). The district judge examined the documents in camera and ruled that some were privileged but others were not. The appeals challenge the latter ruling.

As is generally though not always the case when an appeal challenges the application of a legal rule to the facts (sometimes called a ruling on a "mixed question of fact and

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1. Judge Evans was a member of the original panel that heard oral argument. He recused himself after the argument and has not participated in the decision of the appeal. Chief Judge Posner took his place and listened to the tape of the oral argument, as well as reading the briefs and conferring with the remaining members of the panel.

law," Ornelas v. United States, 517 U.S. 690, 696-97, 134 L. Ed. 2d 911, 116 S. Ct. 1657 (1996); Pullman-Standard v. Swint, 456 U.S. 273, 289 n. 19, 72 L. Ed. 2d 66, 102 S. Ct. 1781 (1982)), our review of the judge's ruling on the privilege claims is deferential; we ask not whether the ruling was erroneous but whether it was clearly erroneous, e.g., In re Teranis, 128 F.3d 469, 471 (7th Cir. 1997); Williams v. Commissioner, 1 F.3d 502, 505 (7th Cir. 1993), just as when we are reviewing simple factfindings. Fed. R. Civ. P. 52(a). Whether a particular document is privileged is a fact-specific and case-specific issue, the sort of issue that district judges are particularly experienced in resolving. It is not the sort of issue that lends itself to governance by a uniform rule that a court of appeals might prescribe and enforce. In these circumstances, a light appellate touch is best.

This is generally the case when the issue on appeal is whether the trial court or jury correctly applied a rule of law to the facts. Such an issue is fact- and case-specific, and so does not lend itself to uniform resolution across different cases, the sort of resolution that requires plenary appellate review. That is why we said in the preceding paragraph that "generally" the standard for reviewing such issues is deferential. Generally is not always, and the exceptions, illustrated by Ornelas, are important. But the only exceptions the Supreme Court has carved are for certain constitutional issues, where the risk of error is thought sufficiently serious to warrant a more searching than normal review for error, and in this circuit, at least, we have been reluctant to recognize exceptions outside the constitutional area. Other courts have not been so austere; it is easy to cite a string of cases in which a court describes the standard of review for a

mixed question of nonconstitutional law and fact, such as fair use in a copyright case or likelihood of confusion in a trademark case; but we are not aware of any case which explains why such an issue requires plenary review, and we cannot think of any respect bearing on the optimal standard of review in which any of these issues differs from the issue of privilege in this case. The presumption in this circuit is and we hope will remain that the clear-error standard is the proper standard for appellate review of determinations of mixed questions of fact and law. This presumption is a helpful simplification of the law of appellate review, with no downside that we can see; and there is certainly nothing in the circumstances of the present case, or the class of cases that it exemplifies (nonconstitutional privilege cases), to rebut it.

Most of the documents in issue were created in connection with Frederick's preparation of the Lenzes' tax returns. They are drafts of the returns (including schedules), worksheets containing the financial data and computations required to fill in the returns, and correspondence relating to the returns. These are the kinds of document that accountants and other preparers generate as an incident to preparing their clients' returns, or that the taxpayers themselves generate if they prepare their own returns, though in the latter case there is unlikely to be correspondence. The materiality of the documents to the IRS's investigation of the Lenzes is not in issue.

There is no common law accountant's or tax preparer's privilege, Couch v. United States, 409 U.S. 322, 335, 34 L. Ed. 2d 548, 93 S. Ct. 611 (1973); United States v. Arthur

Young & Co., 465 U.S. 805, 817-19, 79 L. Ed. 2d 826, 104 S. Ct. 1495 (1984), and a taxpayer must not be allowed, by hiring a lawyer to do the work that an accountant, or other tax preparer, or the taxpayer himself or herself, normally would do, to obtain greater protection from government investigators than a taxpayer who did not use a lawyer as his tax preparer would be entitled to. United States v. Lawless, 709 F.2d 485, 487-88 (7th Cir. 1983); United States v. Bornstein, 977 F.2d 112, 116-17 (4th Cir. 1992); In re Grand Jury Investigation, 842 F.2d 1223, 1224-25 (11th Cir. 1987); United States v. Davis, 636 F.2d 1028, 1043 (5th Cir. 1981). To rule otherwise would be to impede tax investigations, reward lawyers for doing nonlawyers' work, and create a privileged position for lawyers in competition with other tax preparers — and to do all this without promoting the legitimate aims of the attorney-client and work-product privileges. The attorney-client privilege is intended to encourage people who find themselves involved in actual or potential legal disputes to be candid with any lawyer they retain to advise them. Upjohn Co. v. United States, 449 U.S. 383, 389, 66 L. Ed. 2d 584, 101 S. Ct. 677 (1981). The hope is that this will assist the lawyer in giving the client good advice (which may head off litigation, bring the client's conduct into conformity with law, or dispel legal concerns that are causing the client unnecessary anxiety or inhibiting him from engaging in lawful, socially productive activity) and will also avoid the disruption of the lawyer-client relationship that is brought about when a lawyer is sought to be used as a witness against his client. The work-product privilege is intended to prevent a litigant from taking a free ride on the research and thinking of his opponent's lawyer and to avoid the resulting deterrent to a lawyer's committing

his thoughts to paper. United States v. Nobles, 422 U.S. 225, 236-39, 45 L. Ed. 2d 141, 95 S. Ct. 2160 (1975); Hickman v. Taylor, 329 U.S. 495, 510-11, 91 L. Ed. 451, 67 S. Ct. 385 (1947); id. at 516 (Jackson, J., concurring).

Communications from a client that neither reflect the lawyer's thinking nor are made for the purpose of eliciting the lawyer's professional advice or other legal assistance are not privileged. The information that a person furnishes the preparer of his tax return is furnished for the purpose of enabling the preparation of the return, not the preparation of a brief or an opinion letter. Such information therefore is not privileged.

We do not, however, accept the government's argument that there is no issue of privilege here because the information was transmitted to a tax preparer with the expectation of its being relayed to a third party, namely the IRS. It is true that "if the client transmitted the information so that it might be used on the tax return, such a transmission destroys any expectation of confidentiality." United States v. Lawless, supra, 709 F.2d at 487; see also United States v. Windfelder, 790 F.2d 576, 579 (7th Cir. 1986); In re Grand Jury Proceedings, 727 F.2d 1352, 1356 (4th Cir. 1984). That is, the transmittal operates as a waiver of the privilege. But the tax preparer here was also the taxpayers' lawyer, and it cannot be assumed that everything transmitted to him by the taxpayer was intended to assist him in his tax-preparation function and thus might be conveyed to the IRS, rather than in his legal-representation function. Cf. United States v. (Under Seal), 748 F.2d 871, 875-76 (4th Cir. 1984).

We also reject the government's argument that numerical information can never fall within the attorney-client or work-product privilege. Cf. United States v. Schwimmer, 892 F.2d 237, 242 (2d Cir. 1989); United States v. Davis, supra, 636 F.2d at 1043; In re Grand Jury Proceedings, 601 F.2d 162, 171-72 (5th Cir. 1979). Such cases are rare, but they can be imagined. Suppose a lawyer prepared an estimate of his client's damages; the estimate would be numerical, but insofar as it reflected the lawyer's professional assessment of what to ask the jury for it would be attorney work product. Similarly, if the lawyer asked his client how much he had obtained in the theft for which he was being prosecuted and the client answered, "$10,000," the answer would be protected by the attorney-client privilege. But we do not agree with the appellants that the district judge based his ruling on the erroneous view that numbers can never be privileged. He found no basis for privileging these numbers, remarking, rightly, "It cannot be argued that numbers in the hands of the accountant are different from numbers in the hands of a lawyer."

Besides the information supplied to Frederick by the Lenzes, there are the worksheets, which Frederick prepared and which doubtless reflect some of his own thinking. But the Supreme Court has held that an accountant's worksheets are not privileged, United States v. Arthur Young & Co., supra, 465 U.S. at 817-19, and a lawyer's privilege, as we explained earlier, is no greater when he is doing accountant's work. A complicating factor is that when Frederick was doing these worksheets and filling out the Lenzes' tax returns, he knew that the IRS was investigating the Lenzes and their company, albeit in connection with different tax years, and

he was representing them in that investigation. But people who are under investigation and represented by a lawyer have the same duty as anyone else to file tax returns. They should not be permitted, by using a lawyer in lieu of another form of tax preparer, to obtain greater confidentiality than other taxpayers. By using Frederick as their tax preparer, the Lenzes ran the risk that his legal cogitations born out of his legal representation of them would creep into his worksheets and so become discoverable by the government. The Lenzes undoubtedly benefited from having their lawyer do their returns, but they must take the bad with the good; if his legal thinking infects his worksheets, that does not cast the cloak of privilege over the worksheets; they are still accountants' worksheets, unprotected no matter who prepares them.

Put differently, a dual-purpose document — a document prepared for use in preparing tax returns and for use in litigation — is not privileged; otherwise, people in or contemplating litigation would be able to invoke, in effect, an accountant's privilege, provided that they used their lawyer to fill out their tax returns. And likewise if a taxpayer involved in or contemplating litigation sat down with his lawyer (who was also his tax preparer) to discuss both legal strategy and the preparation of his tax returns, and in the course of the discussion bandied about numbers related to both consultations: the taxpayer could not shield these numbers from the Internal Revenue Service. This would be not because they were numbers, but because, being intended (though that was not the only intention) for use in connection with the preparation of tax returns, they were an unprivileged category of numbers.

Appendix A

The most difficult question presented by this appeal, and one on which we cannot find any precedent, relates to documents, numerical and otherwise, prepared in connection with audits of the taxpayers' returns. An example is a memo from Frederick to a paralegal asking her for the amount that Mr. Lenz and his corporation had paid Frederick for legal services rendered personally to Lenz in 1992. The memo was prepared to help Frederick respond to questions raised in an audit of the Lenzes' and the corporation's tax returns. An audit is both a stage in the determination of tax liability, often leading to the submission of revised tax returns, and a possible antechamber to litigation. When a revenue agent is merely verifying the accuracy of a return, often with the assistance of the taxpayer's accountant, this is accountants' work and it remains such even if the person rendering the assistance is a lawyer rather than an accountant. Throwing the cloak of privilege over this type of audit-related work of the taxpayer's representative would create an accountant's privilege usable only by lawyers. If, however, the taxpayer is accompanied to the audit by a lawyer who is there to deal with issues of statutory interpretation or case law that the revenue agent may have raised in connection with his examination of the taxpayer's return, the lawyer is doing lawyer's work and the attorney-client privilege may attach. But the documents in issue do not, so far as we are able to determine, relate to such representation.

We should consider the possible bearing of a new statute, 26 U.S.C. § 7525, which extends the attorney-client privilege to "a federally authorized tax practitioner," that is, a nonlawyer who is nevertheless authorized to practice before the Internal Revenue Service. § 7525(a)(3)(A). Nonlawyers

(including tax preparers, many of them accountants) have long been allowed to practice before it. 5 U.S.C. § 500(c); 31 C.F.R. §§ 10.3, 10.7(c)(viii). The new statute protects communications between a taxpayer and a federally authorized tax practitioner "to the extent the communication would be considered a privileged communication if it were between a taxpayer and an attorney." § 7525(a)(1). (It does not protect work product.) Nothing in the new statute suggests that these nonlawyer practitioners are entitled to privilege when they are doing other than lawyers' work; and so the statute would not change our analysis even if it were applicable to this case, which it is not, because it is applicable only to communications made on or after July 22, 1998, the date the statute was enacted. See Note following 26 U.S.C. § 7525.

We have looked at all the documents that Frederick argues are privileged. Most are dual-purpose documents, about which no more may be said; some were not even submitted to the district judge for consideration of whether they might be privileged; in others as well, privilege was waived. We cannot find any clear errors in the district judge's rulings.

Affirmed.

Appendix A

CONCUR BY: Diane P. Wood

CONCUR: Diane P. Wood, Circuit Judge, concurring. Although I concur in the result the court reaches here, I wish to comment on its initial statement about the proper standard of review in this case. Before concluding that "a light appellate touch" is appropriate for reviewing the district court's decisions about whether particular documents were privileged — a conclusion with which I agree — the court comments that it is "generally" the case that mixed questions of law and fact are reviewed under the clearly erroneous standard. That statement is neither here nor there for this case, since we are all agreed that a deferential standard applies on these facts. But I am concerned that it is too sweeping and could lead to error in cases requiring a more nuanced appellate review of mixed questions.

As the majority notes, the appropriate standard of review for mixed questions of law and fact is not the same in all cases, and thus this is not a question that lends itself to uniform resolution across different cases. Ante at 3. With that much, I am in full agreement. I note here that this statement, coupled with the observation that the character of documents as privileged or not privileged is a highly fact-specific inquiry for which the clearly erroneous standard is proper, is enough to decide the case before us. The majority goes on, however, to speculate that one can discern a "presumption" in the cases decided within this circuit in favor of clear error review for mixed questions of law and fact. With respect, I think this overstates the case considerably.

Some background is important to understand the way in which mixed questions have in fact been treated in this court

and elsewhere. Prior to Ornelas v. United States, 517 U.S. 690, 134 L. Ed. 2d 911, 116 S. Ct. 1657 (1996), this court occasionally made sweeping statements along the lines of the majority's opinion today. See, e.g., Baldwin v. United States, 60 F.3d 363, 365 (7th Cir. 1995) ("This court . . . has moved decisively to the position that appellate review of determinations of mixed questions of fact and law should be governed by the standard of clear error, and not by the de novo standard.") (internal citations omitted), vacated, 517 U.S. 1231 (1996); see also Mucha v. King, 792 F.2d 602, 605 (7th Cir. 1986) ("[M]ost courts treat legal characterizations (negligence, possession, ratification, principal place of business, etc.) as facts to which the clearly-erroneous standard applies. That is certainly the view of this circuit.") (internal citations omitted); see generally Evan Tsen Lee, Principled Decision Making and the Proper Role of Federal Appellate Courts: The Mixed Questions Conflict, 64 S. Cal. L. Rev. 235, 240-41 (1991) (discussing the Seventh Circuit's approach to mixed questions as "following the rule stated in Mucha v. King without regard to the particular type of mixed question."). But in Ornelas, the Supreme Court reversed our use of the clear error standard to review a district court's determination of probable cause and reasonable suspicion, and the Court underscored the point by vacating the judgment in Baldwin, supra, as well, in light of Ornelas. Since then, we have rightly exercised more caution in our choice of the proper standard for mixed questions. See In re Krehl, 86 F.3d 737, 742 (7th Cir. 1996).

The majority concedes that Ornelas is not consistent with its idea of a presumption in favor of clear error review, but it attempts to distinguish Ornelas and the cases in this circuit

that have followed its methodology by observing that they typically implicate constitutional rights. It is true that one can find recent examples from this court that recognize the need for review more searching than clear error, in which the legal principle at stake came from the Constitution. So, for example, we explained in one case that "most mixed questions of law and fact that require the application of constitutional principles to historical fact receive de novo review." Coulter v. Gilmore, 155 F.3d 912, 917 (7th Cir. 1998), citing Ornelas v. United States, 517 U.S. at 697-99 and Thompson v. Keohane, 516 U.S. 99, 111-12, 133 L. Ed. 2d 383, 116 S. Ct. 457 (1995); see also, e.g., United States v. Raszkiewicz, 169 F.3d 459, 1999 WL 74692, at *2 (7th Cir. 1999) (reviewing de novo the mixed question of whether defendant was denied the right to a jury selected from a cross-section of the community); Mahaffey v. Page, 162 F.3d 481, 484 (7th Cir. 1998) (reviewing de novo the mixed question of whether defendant made a prima facie case of a Batson violation). But the source of the law that contributes the legal component to the "mixed" question logically has nothing to do with the depth of appellate review. Examples abound of courts that apply a stricter standard of review than clear error to mixed questions that do not implicate the Constitution. See, e.g., Indest v. Freeman Decorating, Inc., 168 F.3d 795, 1999 WL 98505, at *8 (5th Cir. 1999) (sexual harassment); Nihon Keizai Shimbun, Inc. v. Comline Bus. Data, Inc., 166 F.3d 65, 72 (2d Cir. 1999) (fair use of a copyrighted work); Jet, Inc. v. Sewage Aeration Sys., 165 F.3d 419, 422 (6th Cir. 1999) (likelihood of confusion in trademark infringement action); Hoover v. Morales, 164 F.3d 221, 224 (5th Cir. 1998) (grant of a preliminary injunction); United States v. Moore, 159 F.3d 1154, 1157 (9th Cir. 1998) (conflict of interest of

trial counsel); Brink's Ltd. v. South African Airways, 149 F.3d 127, 132 (2d Cir. 1998) (wilful misconduct under the Warsaw Convention).

In my view, therefore, it is at best unhelpful and at worst misleading to claim that a single standard of review "generally" applies to mixed questions, or that there is some kind of "presumption" in non-constitutional cases. We are required instead to engage in the type of nuanced, policy-driven analysis the Supreme Court outlined in Ornelas. There the Court examined its past practice, the need for appellate courts to ensure a unitary system of law, the fact that the legal principles at issue acquired their content only through application to fact patterns, and the tendency of de novo review to unify precedent. 517 U.S. at 697-99. In other cases, the Court has considered the district court's superior fact-finding capabilities and whether searching appellate review would clarify legal doctrine. Salve Regina College v. Russell, 499 U.S. 225, 233, 113 L. Ed. 2d 190, 111 S. Ct. 1217 (1991); Pierce v. Underwood, 487 U.S. 552, 559-60, 101 L. Ed. 2d 490, 108 S. Ct. 2541 (1988); Miller v. Fenton, 474 U.S. 104, 114, 88 L. Ed. 2d 405, 106 S. Ct. 445 (1985). Only if we, too, engage in a careful review of these factors when selecting a standard of review for each different type of mixed question can we perform our proper function of expounding the law and assuring its uniform application.

In this case, the clear error standard is the right choice for the reasons I have identified: only the underlying facts about the documents are really at issue (i.e., who said what to whom, was the document written for the purpose of preparing tax returns, in what capacity did Frederick operate).

Without flagging it, however, the majority has also made an important legal ruling that affected its review: dual-purpose documents are not privileged. This principle can be expressed without regard to the specific facts of a given case, including this one. Because it was easy enough to dissect this general legal principle out from the facts, it was also easy to apply clear error review to the factual components of the privilege question. Even if the question is theoretically a "mixed" one, clear error review is the appropriate choice whenever the appellate court is able cleanly to separate and focus its attention exclusively on the factual findings that lie behind the mixed question. When the meaning of the law (constitutional or otherwise) cannot be separated from the significance of the facts, however, Ornelas requires us to apply de novo review. This is not a choice that can be made in the abstract, or through presumptions. Only a careful analysis of each case will enable us to make the proper choice.

APPENDIX B — DECISION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WISCONSIN DATED AND FILED FEBRUARY 12, 1998

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WISCONSIN

Civil Action No. 94-C-1281

UNITED STATES OF AMERICA,

Petitioner,

v.

RICHARD A. FREDERICK,

Respondent,

– and –

RANDOLPH W. LENZ, KARIN LENZ, and KCS INDUSTRIES, INC.,

Respondent-Intervenors.

DECISION AND ORDER

The government filed this action to enforce two summonses issued by the Internal Revenue Service to respondent Richard Frederick ("Frederick"), an attorney for respondent-intervenors Randolph W. Lenz and Karin Lenz.

Frederick has also represented respondent-intervenor KCS Industries, Inc. ("KCS"),[1] in the past. The court will collectively refer to Frederick, the Lenzes, and KCS as "Respondents." The summonses, which sought Frederick's 1988 to 1992 records related to the Lenzes and their business dealings, were issued pursuant to 26 U.S.C. § 7602. While producing close to 7,000 pages of documents, Frederick withheld just over 800 based on attorney-client privilege and the work product doctrine. More documents have since been disclosed by Frederick, and there are approximately 90 documents before the court for *in camera* review.

This court's August 19, 1996 decision and order contains a detailed description of the factual background of this action. Frederick, a tax attorney, was first retained by the Lenzes in the early 1980s to represent them with respect to audits of their 1976-1979 tax returns. (May 26, 1995 Frederick Aff. ¶ 6.) For every subsequent year, the Internal Revenue Service has audited one of the Lenzes' personal returns or the return of a business entity associated with Mr. Lenz, and Frederick has represented the Lenzes in a number of these audits. (*Id.* ¶ 7.) Frederick has prepared the Lenzes' personal tax returns since 1981. (*Id.* ¶ 10.)

DISCUSSION

The court has scrutinized each document which Respondents seek to withhold from the Internal Revenue Service. In addition to the parties' memoranda, the court has reviewed a document inventory prepared by Respondents,

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1. Mr. Lenz was the chairman and chief executive officer of KCS.

Appendix B

Frederick's affidavit, and an appendix accompanying Frederick's affidavit which contains Frederick's document-by-document discussion, which was filed under seal ("App." or "Appendix").

Attorney-Client Privilege: General Principles

The attorney-client privilege is defined as follows:

> (1) Where legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal adviser, (8) except the protection be waived.

United States v. Evans, 113 F.3d 1457, 1461 (7th Cir. 1997) (quoting 8 John Henry Wigmore, Evidence in Trials at Common Law § 2292 (John T. McNaughton rev. 1961)). Respondents, as the parties seeking to invoke the protection of the attorney-client privilege, have the burden of proving the elements of the privilege. *Id.* The privilege must be analyzed as to each document; legal conclusions are inadequate, and specific facts must be alleged. *Holifield v. United States*, 909 F.2d 201, 204 (7th Cir. 1990). Facts supported by affidavit must be supplied to establish all elements of the privilege. *Id.* (citing *United States v. First State Bank*, 691 F.2d 332 (7th Cir. 1982)).

With respect to attorneys who prepare tax returns, the Seventh Circuit has stated that "[t]he attorney must be acting

in his capacity as a professional legal adviser at the time the information was transferred. Several courts have held that the preparation of a tax return, while it may require some knowledge of the law, is primarily an accounting service." *United States v. Lawless*, 709 F.2d 485, 487 (7th Cir. 1983) (citations omitted). "If the client transmitted the information so that it might be used on the tax return, such a transmission destroys any expectation of confidentiality which might have otherwise existed." *Id.* "[D]isclosure of tax information effectively waives the privilege 'not only to the transmitted data but also as to the details underlying that information.' " *Id.* at 488 (citation omitted); *see also United States v. Windfelder*, 790 F.2d 576 (7th Cir. 1986).

Work Product Doctrine: General Principles

The Supreme Court first recognized the work product doctrine in *Hickman v. Taylor*, 329 U.S. 495 (1947). The doctrine is applicable to summonses issued by the Internal Revenue Service. *Upjohn Co. v. United States*, 449 U.S. 383 (1981).

Documents may be protected by the work product doctrine if they were " 'prepared or obtained *because* of the prospect of litigation.' " *Logan v. Commercial Union Ins. Co.*, 96 F.3d 971, 976-77 (7th Cir. 1996) (citation omitted). " '[T]he primary motivating purpose behind the creation of a document . . . must be to aid in possible future litigation.' " *Binks Mfg. Co. v. National Presto Indus., Inc.*, 709 F.2d 1109, 1119 (7th Cir. 1983) (citation omitted). Respondents have the burden of proving that the documents for which the work

product doctrine is claimed were created in anticipation of litigation. *See id.*

Non-Privileged Documents: Accounting Capacity

As discussed above, the fact that Frederick is an attorney does not mean that the work he performs in an accounting capacity is privileged. Frederick has acted both as accountant and attorney; to receive the protection they seek, Respondents must establish that the documents were created by Frederick in his capacity as a lawyer, and if the work product doctrine is claimed, that the documents were prepared in anticipation of litigation. The court finds that the following documents are those which would be created by an accountant, and therefore are not privileged: FPR-000414; FPR-000416 and FPR-000417[2]; FPR-000418; FPR-000419; FPR-000420; FPR-000421; FPR-000422; FPR-000423 and FPR-000424; FPR-000425; FPR-000426 and FPR-000427; FPR-000428 and FPR-000429; FPR-000430; FPR-000431; FPR-000432[3]; FPR-000484[4];

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2. The attorney-client privilege has also been waived as to these documents. See discussion section entitled "Non-Privileged Documents: Attorney-Client Privilege Waived."

3. The court observes that there are handwritten notes on this document, for which there is no specific discussion in Frederick's affidavit or the Appendix. (See App. at 3-4, ¶ 2.)

4. The Appendix lumps the explanation of this document with FPR-000486, and contains no explanation regarding how this document wits a communication between Frederick and Mr. Lenz. (App. at 12-13, ¶ 2). The Appendix's explanation that this document contains Frederick's legal analysis does not fit with the contents of the document, nor does it establish that the document was created in anticipation of litigation. (*Id.*)

FPR-000496[5]; FPR-100217; FPR-100218; FPR-100219; FPR-100220; FPR-100221; FPR-100222; FPR-100223; FPR-100224; FPR-100225; FPR-100229[6]; P-0005469; P-0005470; P-0005471 and P-0005472; P-0005473; P-0005474, P-0005475, and P-0005476[7]; P-0005477 and P-0005478; P-0005479 and P-0005480; P-0005482[8]; P-0006494 and P-0006495[9]; P-0006499 and P-0006500; and P-0006501 and P-0006502.[10]

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5. This document is attached to FPR-000495, a fax cover sheet which was not marked confidential although that designation was available. See discussion section entitled "Non-Privileged Documents: Miscellaneous." The Appendix states that Frederick discussed confidential matters with the recipient, but does not explain how those confidential matters are contained in this document.

6. The attorney-client privilege has also been waived as to this document. See discussion section entitled "Non-Privileged Documents: Attorney-Client Privilege Waived."

7. The Appendix contains no discussion of the attorney-client privilege with respect to these documents. The attorney-client privilege has also been waived as to these documents. See discussion section entitled "Non-Privileged Documents: Attorney-Client Privilege Waived."

8. The Appendix contains no discussion of the attorney-client privilege with respect to this document.

9. The Appendix contains no discussion of the attorney-client privilege with respect to this document.

10. These documents are identical to P-0006499 and P-0006500.

Appendix B

Non-Privileged Documents: Attorney-Client Privilege Waived

There are a number of documents for which there is no discussion in Frederick's affidavit or the Appendix regarding the nature of the relationship between the individual who Frederick is interacting with, and Mr. Lenz or the business entity which the Appendix asserts holds the attorney-client privilege. The court therefore cannot determine whether the privilege was waived by disclosing the document to a third party who is not a client for purposes of the privilege. *See Upjohn Co. v. United States*, 449 U.S. 383 (1981). The documents for which Respondents have failed to meet their burden in this regard are: FPR-000415; FPR-000416 and FPR-000417[11]; FPR-100129[12]; FPR-100195[13]; FPR-100196[14]; FPR-100229[15]; and P-0005474, P-0005475, and P-0005476.[16]

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11. These documents are also not privileged because they were prepared in an accounting capacity. See discussion section entitled "Non-Privileged Documents: Accounting Capacity."

12. The court also finds that this document is not protected by the work product doctrine.

13. *See also* Discussion section entitled "Non-Privileged Documents: Miscellaneous."

14. The court finds that this document is protected by the work product doctrine. (App. at 15-16, ¶ 8.)

15. This document is also not privileged because it was prepared in an accounting capacity. See discussion section entitled "Non-Privileged Documents: Accounting Capacity." The court also finds that this document is not protected by the work product doctrine.

16. These documents were created in an accounting capacity. See discussion section entitled "Non-Privileged Documents: Accounting Capacity." The court also finds that these documents are not protected by the work product doctrine.

Appendix B

Non-Privileged Documents: Miscellaneous

Respondents have failed to meet their burden of establishing that the following documents are protected by either the attorney-client privilege or the work product doctrine.

FPR-000495. This document is a fax cover sheet to an attorney at KCS who also worked for Mr. Lenz. The attorney-client privilege is claimed. The document is not marked confidential on the line available for such designation. (There is an instruction on the cover sheet which reads "IF MARKED CONFIDENTIAL, PLEASE PLACE IN A CONFIDENTIAL ENVELOPE.") The document contains standard cover sheet information such as names and phone numbers, and no confidential information on its face.

FPR-000540. This document is handwritten notes by Frederick. The attorney-client privilege is claimed. The description in the Appendix does not fit the document. (App. at 14, ¶ 5.)

FPR-100180[17], FPR-100181, FPR-100182, FPR-100183, FPR-100184, FPR-100185, FPR-100186, FPR-100187, FPR-100188, FPR-100189, FPR-100190, FPR-100191,

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17. This document is a memorandum from Frederick's paralegal to Frederick. The attorney-client privilege and work product doctrine are claimed. There is no explanation regarding how the document is a communication between Frederick and one of his clients, so the attorney-client privilege is not available. (App. at 20, ¶ 2.) The court also finds that the document is not protected by the work product doctrine.

FPR-100192, FPR-100193, and FPR-100194.[18] These documents are memoranda and copies of billing statements from Frederick. The attorney-client privilege and work product doctrine are claimed. The general rule is that information regarding attorney fees is not privileged. *In the Matter of Grand Jury Proceeding*, 898 F.2d 565, 567 (7th Cir. 1990). There is no explanation regarding how the documents are confidential communications with one of Frederick's clients, so the attorney-client privilege is not available. (App. at 20, ¶ 2.) There is no discussion by Respondents of any legal authority relevant to this issue.

FPR-100195. This document, apparently an attachment to FPR-100194, is a spreadsheet. The attorney-client privilege and work product doctrine are claimed. There is no explanation regarding how the document is a communication with one of Frederick's clients, so the attorney-client privilege is not available. (App. at 20, ¶ 2.) There also is a Post-It™ indicating that the document was faxed to an individual identified only by name. The attorney-client privilege has also been waived as to these documents. See discussion section entitled "Non-Privileged Documents: Attorney-Client Privilege Waived." The court also finds that the document is not protected by the work product doctrine.

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18. This document is a memorandum from Frederick to his paralegal, and a responding memorandum from Frederick's paralegal to Frederick. The attorney-client privilege and work product doctrine are claimed. There is no explanation regarding how the document is a communication with one of Frederick's clients, so the attorney-client privilege is not available. (App. at 20, ¶ 2.) The court also finds that the document is not protected by the work product doctrine.

FPR-100228. This document is a cover letter from Frederick to Mr. Lenz. The attorney-client privilege and work product doctrine are claimed. Respondents' document inventory states that the letter contains legal advice, but it does not on its face. The Appendix explains that this document references in enclosure which is work product, but the substance of the enclosure is not revealed by the cover letter. (App. at 19.)

P-0006497. This document is a brokerage statement. Respondents seek to redact handwritten notes at the bottom of the document. The attorney-client privilege and work product doctrine are claimed. The notes are not legal in nature and there is no identification as to who wrote them (they are dissimilar in writing style from other notes by Frederick).

P-0006498. This document is a brokerage statement. Respondents seek to redact handwritten notes contained on a Post-It™ on the document. The attorney-client privilege and work product doctrine are claimed. The court's copy of this document does not have a Post-It™, so the court must conclude that this document is not protected by the attorney-client privilege and/or the work product doctrine.

Privileged Documents

The court finds that the following documents are protected by the attorney-client privilege and/or the work product doctrine. The parenthetical following each document indicates whether the attorney-client privilege and/or the work product doctrine applies, and the portion of the Appendix upon which the court is relying to reach its conclusions.

FPR-000485 (attorney-client privilege and work product doctrine (App. at 13, ¶ 3)); FPR-000486 (attorney-client privilege and work product doctrine (App. at 12-13, ¶ 2)); FPR-000538 (attorney-client privilege (App. at 13-14, ¶ 4)); FPR-000539 (attorney-client privilege (App. at 13-14, ¶ 4)); FPR-000541 (attorney-client privilege (App. at 14, ¶ 5)); FPR-100037 (attorney-client privilege (App. at 20, ¶ 1)); FPR-100127 (attorney-client privilege and work product doctrine (App. at 14-15, ¶ 6)); FPR-100130 (attorney-client privilege and work product doctrine (App. at 15, ¶ 7)); FPR-100131 (attorney-client privilege and work product doctrine (App. at 15, ¶ 7)); FPR-100134, FPR-100135, and FPR-100136 (attorney-client privilege (App. at 17-18, ¶ 4)); FPR-100196 (work product doctrine (App. at 15-16, ¶ 8)); FPR-100216 (attorney-client privilege and work product doctrine (App. at 18, ¶ e)); P-0005481 (attorney-client privilege and work product doctrine — the paragraphs numbered fourteen, fifteen, and sixteen may be redacted (App. at 24, ¶ 8)); and P-0006496[19] (attorney-client privilege and work product doctrine — handwritten notes may be redacted (App. at 25, ¶ 10)).

CONCLUSION

Respondent Richard A. Frederick and/or Respondents-Intervenors Randolph W. Lenz, Karin Lenz and KCS Industries, Inc. have not carried their burden of establishing that the following documents should not be disclosed to petitioner United States of America on the grounds of

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19. This document is mistakenly identified as P-006499 in Respondents' document inventory.

attorney-client privilege and/or the work product doctrine: FPR-000414; FPR-000415; FPR-000416 and FPR-000417; FPR-000418; FPR-000419; FPR-000420; FPR-000421; FPR-000422; FPR-000423 and FPR-000424; FPR-000425; FPR-000426 and FPR-000427; FPR-000428 and FPR-000429; FPR-000430; FPR-000431; FPR-000432; FPR-000484; FPR-000495; FPR-000496; FPR-000540; FPR-100129; FPR-100180, FPR-100181, FPR-100182, FPR-100183, FPR-100184, FPR-100185, FPR-100186, FPR-100187, FPR-100188, FPR-100189, FPR-100190, FPR-100191, FPR-100192, FPR-100193, FPR-100194, and FPR-100195; FPR-100196; FPR-100217; FPR-100218; FPR-100219; FPR-100220; FPR-100221; FPR-100222; FPR-100223; FPR-100224; FPR-100225; FPR-100228; FPR-100229; P-0005469; P-0005470; P-0005471 and P-0005472; P-0005473; P-0005474, P-0005475, and P-0005476; P-0005477 and P-0005478; P-0005479 and P-0005480; P-0005482; P-0006494 and P-0006495; P-0006497; P-0006498; P-0006499 and P-0006500; and P-0006501 and P-0006502. The Internal Revenue Service summonses with respect to the preceding documents shall be enforced. Respondent Richard A. Frederick shall disclose the preceding documents to petitioner United States of America.

Respondent Richard A. Frederick and/or Respondents-Intervenors Randolph W. Lenz, Karin Lenz and KCS Industries, Inc., have carried their burden of establishing that the following documents should not be disclosed to petitioner United States of America on the grounds of attorney-client privilege and/or the work product doctrine: FPR-000485; FPR-000486; FPR-000538; FPR-000539; FPR-000541;

FPR-100037; FPR-100127; FPR-100130; FPR-100131; FPR-100134, FPR-100135, and FPR-100136; FPR-100196; FPR-100216; P-0005481 (the paragraphs numbered fourteen, fifteen, and sixteen may be redacted); and P-0006496 (handwritten notes may be redacted). The Internal Revenue Service summonses with respect to the preceding documents shall not be enforced.

On or before twenty days from the date of this order, petitioner United States of America shall serve and file a written statement or other appropriate document regarding how it requests this court to proceed to close this action.

On or before twenty days from service of petitioner's statement, respondent Richard Frederick and respondent-intervenors Randolph W. Lenz, Karin Lenz, and KCS Industries, Inc., shall serve and file a response.

SO ORDERED this 12th day of February, 1998.

s/ John W. Reynolds
John W. Reynolds
United States District Judge

APPENDIX C — DECISION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WISCONSIN DATED AND FILED AUGUST 19, 1996

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WISCONSIN

Civil Action No. 94-C-1281

UNITED STATES OF AMERICA,

Petitioner,

v.

RICHARD A. FREDERICK,

Respondent,

– and –

RANDOLPH W. LENZ, KARIN LENZ, and KCS INDUSTRIES, INC.,

Respondent-Intervenors.

DECISION AND ORDER

BACKGROUND

When do the attorney-client privilege or the work product doctrine trump the statutory power of the Internal

Revenue Service (IRS) to discover the records of a tax attorney resisting an IRS summons? This dispute is a clash between the power of the Government to compel a party to comply with an IRS summons, and the common-law recognition of the sacredness of communications between attorney and client. Accountants have no privileges. The wrinkle in this case is that the respondent wears both the accountant hat and the attorney hat. The court certainly cannot allow taxpayers to stifle Internal Revenue Service investigations by providing tax attorneys a blanket privilege for all information they receive or generate. Conversely, the court cannot give the Government a carte blanche right to discover every document just because a party's attorney also does tax returns. However, there is no puzzle; the same analysis applies to this situation as any other when a privilege is asserted.

Richard Frederick (Frederick), the respondent, is a tax attorney for Karin and Randolph Lenz, two of the respondent-intervenors.[1] The IRS issued summonses pursuant to I.R.C. § 7602 for Frederick's records from 1988 to 1992, as they related to the Lenzes and their business dealings. Frederick provided the IRS with several thousand documents but withheld several hundred arguing that the documents were protected by the attorney-client privilege and the work product doctrine. Over time the parties have narrowed the number of documents requested.

In May 1995, the parties, including Frederick and the respondent-intervenors (collectively the "respondents") filed

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1. Mr. Lenz used to be the chairman and chief executive officer of KCS Industries, Inc., the third respondent-intervenor.

cross motions on the issue of whether the court could summarily enforce the IRS summonses. The court will grant the Government's motion with regard to draft documents and worksheets except where there are additional communications reflected on the documents. The court will deny the motion for summary enforcement on the remaining documents. The respondents have moved to seal the appendix to Frederick's affidavit. It contains a description of all the documents in question. The court will deny respondents' motion. After reviewing the affidavit, the petitioner will inform the court which documents, if any, it still wants to discover. At that point in time, the court will schedule an *in camera* review of these documents.

FACTS

The facts are not in dispute. Richard Frederick is a tax attorney in private practice in Milwaukee, Wisconsin. He provides tax advice to corporations and individuals, assesses the tax consequences of real estate and corporate transactions, represents clients in IRS examinations and audits, litigates on clients' behalf in tax and other federal courts, and prepares income tax and other tax filings. (Frederick Aff. at 3.)

Lenz specializes in turning around financially troubled organizations. He is currently the Chairman of the Board of Directors of the Terex Corporation (Terex), a manufacturer of heavy duty construction equipment and trucks, and was, until recently, Chairman and Chief Executive Officer of KCS, a management services company. (*Id.* at 5.) Additionally, Lenz has interests in FWD Corp. (FWD), a fire equipment manufacturer, Corsta Corp., an investment company; Alass

Investment Partners (Alass), an investment limited partnership; Seagrave Racing, Inc. (Seagrave), a vintage race car investment firm; and Corsta Yacht Charters, Inc. (Corsta Yacht), a yacht chartering company. (*Id.*)

For over 15 years, Frederick, acting as an attorney, has represented the Lenzes and entities associated with them in a variety of contexts. He has also provided tax planning advice to the Lenzes and their children, and represented them in real estate transactions, corporate transactions, and lawsuits against private parties. (*Id.* at 6.)

The Lenzes first retained Frederick in the early 1980's to represent them after learning that their 1976-1979 tax returns were being audited. *Id.* Subsequently, the Lenzes directed Frederick to prepare their income tax returns, which Frederick has done since 1981. (*Id.* at 10.) The Lenzes were also audited in 1984 and 1986-88. These audits resulted in Tax Court litigation. Seven of the Lenz's businesses have also been audited. The 1986 and 1987 audits of Corsta Yacht resulted in Tax Court litigation. Since 1993, the Lenzes have been the subject of a criminal tax investigation. (Resp'ts Joint Mem. of Law in Opp'n to Pet'r's Mot. at 2.)

The first IRS summons, served on February 4, 1993, directed Frederick to testify and produce certain documents and records for examination. The summons covered the four tax years from 1988-1991 and asked for all records used in the preparation of the Lenzes' tax returns. Frederick appeared before IRS Special Agent James Hill on June 8, 1993, and produced several thousand pages of records in response to the summons. Hill interviewed Frederick. Frederick refused

to answer certain questions on the grounds that the questions called for information protected by the attorney-client privilege, work product doctrine, or both.

On October 1, 1993, Frederick provided additional records and a privilege log. The log identified the documents that Frederick withheld from production. On December 1, 1993, Frederick provided a supplemental privilege log referencing additional records. A total of 806 pages were withheld. Additionally, Frederick redacted portions of 14 pages of documents on the grounds that the information was nonresponsive or protected by a privilege.

The IRS served a second summons on June 22, 1994, directing Frederick to testify and produce documents relating to his preparation of the Lenzes' 1992 return, any tax work Frederick may have done, and all documents relative to Mr. Lenzes' financial transactions.

On November 16, 1994, the Government filed its petition to enforce both summonses. On December 7, 1994, Frederick produced 811 pages of documents in response to the second summons. He also provided a privilege log detailing the documents to which privilege was being claimed. Frederick also provided a redaction log. Frederick filed his answer to the Government's petition on January 31, 1995. On February 7, 1995, the respondent-intervenors, KCS Industries and the Lenzes, moved to intervene. The court granted that motion.

The parties have narrowed the scope of the documents they want the court to consider. At issue are about 70 documents. (Frederick Aff., App.) Those documents can be

broken down into six categories: draft returns and other tax forms, draft worksheets, handwritten notes, letters and faxes, memoranda, and redacted documents.

ANALYSIS

The Internal Revenue Code provides the Internal Revenue Service (IRS) the authority to issue summonses to gather information pursuant to an investigation of a tax liability. I.R.C. § 7602. Where a party refuses to comply with or otherwise challenges an IRS summons, the Government may apply to the United States District Court for an order compelling compliance with the summons. I.R.C. § 7604(b). The Government must show that 1) the investigation is for a legitimate purpose; 2) the information sought might be relevant to that purpose; 3) the information sought is not already within the Commissioner's possession; and 4) the administrative steps required by the Internal Revenue Code have been followed. *United States v. Berg*, 20 F.3d 304, 308 (7th Cir. 1994). This is a very light burden. The affidavit of an IRS agent investigating the case is generally sufficient to satisfy the four elements. *United States v. Kis*, 658 F.2d 526, 536 (7th Cir. 1981), *cert. denied sub nom.* The Government has met its initial burden by filing the affidavit of Special Agent James Hill. The respondents do not dispute the validity of the summons. What is in dispute is whether the respondents' claims of protected communications are sufficient to defeat the petitioner's requests.

Appendix C

Attorney-Client Privilege & Work Product Doctrine

The respondents assert both the attorney-client privilege and the attorney work product doctrine. The purpose of each is to protect the sanctity of parties in the adversarial system. The attorney-client privilege, by protecting communications made by a party to his or her attorney, encourages parties to make full disclosures to their attorneys. The work product doctrine protects those documents and communications reflecting the mental impressions of an attorney preparing for litigation.

There are eight elements to the attorney-client privilege: 1) Where legal advice of any kind is sought, 2) from a professional legal adviser in his or her capacity as such, 3) the communications relating to that purpose, 4) made in confidence 5) by the client, 6) are at his or her instance permanently protected, 7) from disclosure by the client or legal advisor, 8) except where it is waived. *United States v. Lawless*, 709 F.2d 485, 487 (7th Cir. 1983). The party invoking the privilege has the burden of establishing the elements on a document-by-document basis. *Id.* An IRS summons may be challenged by a claim of attorney-client privilege. *United States v. First State Bank*, 691 F.2d 332, 334 (7th Cir. 1982). However, no accountant-client privilege exists. *Couch v. United States*, 409 U.S. 322, 335 (1973). Information transmitted for the purpose of tax return preparation is not privileged. *United States v. Winfelder*, 790 F.2d 576 (7th Cir. 1986). The privilege is waived in this instance to the information and the "details underlying that information." *Lawless*, 709 F.2d at 488. The privilege only protects those disclosures necessary to obtain legal advice

which might not have been made absent the privilege. *Fisher v. United States*, 425 U.S. 391, 403 (1976). Finally, and perhaps most importantly, the privilege is to be construed narrowly. *United States v. White*, 970 F.2d 328, 334 (7th Cir. 1992) ("the privilege is in derogation of the search for truth . . . and this circuit has repeatedly held that it must be strictly construed.")

In this instance, the court's task is to determine which — if any — documents reflect confidential communications made based on Frederick's role as an attorney, and those communications made based on Frederick's role as an accountant. Respondents have filed, under seal, an appendix listing the documents at issue and an explanation as to why each is privileged. There are six categories: 1. "Draft Returns and other Tax Forms," 2. "Draft Worksheets," 3. "Handwritten Notes," 4. "Letters and Faxes," 5. "Memoranda," and 6. "Redacted Documents." With three exceptions, the court will grant the petitioner's motion with regard to all items listed as "Draft Returns and other Tax Forms" and "Draft Worksheets." The three excluded documents include, in addition to numerical data, written comments that could reflect confidential communications or mental impressions, and thus will require an *in camera* review. The remaining documents in these categories contain numerical information, not confidential communication. Although inferences might be drawn from discrepancies between tax forms and returns actually filed and the draft returns, these are only numerical inferences. Numbers reflect information reported to an accountant but not confidential communication between a client and attorney. Thus, these documents are not protected. It is important to remember

that the scope of the privilege is very narrow. Here, respondents fail to meet their burden; potential inferences of confidential communication are not enough to warrant the privilege.

Respondents' argument that these documents are work product fails. The work product doctrine protects mental impressions, legal theories and analysis that a lawyer makes in anticipation of litigation. *Hickman v. Taylor*, 329 U.S. 495 (1947); Fed. R. Civ. P. 26(b)(3). It may be asserted against enforcement of an IRS summons. *Upohn Co. v. United States*, 449 U.S. 383 (1981). Here, the draft worksheets and tax returns reflect numerical, accounting calculations but not legal theories. They reflect the work of an accountant, not a lawyer. It cannot be argued that numbers in the hands of the accountant are different from numbers in the hands of a lawyer. Thus, those draft returns and worksheets that do not contain written notations are not protected by the work product doctrine.

The remaining documents contain written notations and communications which may reflect Frederick's mental impressions or legal theories. They could reflect confidential communications or work product, thus the court will not grant summary enforcement of the IRS summons without viewing them. Of course, the burden is still on the respondents to show that these documents are the mental impressions of an attorney prepared in anticipation of litigation and not just prepared in the ordinary course of business, or that they are protected by the attorney-client privilege.

For these reasons, the court **GRANTS** the motion with respect to the documents listed in footnote 2 and **DENIES** the motion with regards to the remaining documents.[2]

Respondents have moved to file their appendix under seal. After reviewing the appendix, the court concludes that it, in itself, does not reflect confidential communications. The court **DENIES** respondents' motion to submit the appendix under seal.

The court orders the clerk to forward copies of the respondent's appendix and the respondent-intervenors' appendix (both filed May 26, 1995) to the petitioner.

The petitioner will inform the court within thirty (30) days of the date of this order which documents, if any, it still wants to hold subject to the summons. Those documents should be turned over to the court by the respondents for an *in camera* review.

SO ORDERED this 19th day of August, 1996.

s/ John W. Reynolds
John W. Reynolds
United States District Judge

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2. FPR-433-443, FPR-444-468, FPR-469, FPR-470-483, FPR-494, FPR-497-498, FPR-499-500, FPR-502-508, FPR-509-526, FPR-527-528, FPR 529-534, FPR-568-602, FPR-603-616, FPR-100000-100036, FPR-487, FPR-501, FPR-490, FPR-491, FPR-492, FPR-493, FPR-535, FPR-536, FPR-537, FPR-618, FPR-100038-100068, FPR-100069-100071, FPR-100072-100073, FPR-100074-100097, FPR-100098-100110, FPR-100111-100122, FPR-100128, FPR-100197-100215. These are found in respondents' appendix as 1.c. — i., 1.k., and 2.a. — d.

APPENDIX D — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DENYING PETITION FOR REHEARING DATED JULY 26, 1999

United States Court of Appeals
For the Seventh Circuit
Chicago Illinois 60604

July 26, 1999

Before
Hon. Richard A. Posner, Chief Judge
Hon. Michael S. Kanne, Circuit Judge
Hon. Diane P. Wood, Circuit Judge

Nos. 98-2644 and 98-2700

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

RICHARD A. FREDERICK,

Defendant-Appellant,

and

RANDOLPH W. LENZ, KARIN LENZ, AND KCS INDUSTRIES, INC.,

Intervening Defendants-Appellants.

Appendix D

Appeal from the United States District Court for the Eastern District of Wisconsin

No. 94 C 1281

John W. Reynolds, *Judge.*

ORDER

On June 14, 1999, appellant and intervenor-appellants filed a petition for rehearing with suggestion for rehearing *en banc* and on July 7, 1999, appellee filed an answer. All the judges on the original panel have voted to deny the petition, and none of the active judges has requested a vote on the suggestion for rehearing *en banc*. The petition is therefore **DENIED**.

APPENDIX E — ATTACHMENT TO IRS SUMMONS, DATED FEBRUARY 4, 1993

In Re: Randolph W. and Karin Lenz
30 Compass Point
FT. Lauderdale, FL 33308

All records in your possession or control relating to tax work performed for Randolph W. and Karin Lenz, SSN's: 388-48-2573 and 391-56-0917, respectively, for the years 1988, 1989, 1990 and 1991. Records are to include but not be specifically limited to income tax returns, workpapers, notes, correspondence and copies of or original records furnished to assist in the preparation of the income tax returns, Form 1040, for the periods described.

Notes, workpapers, correspondence, memorandum and copies of or original records furnished by Randolph W. and Karin Lenz for purposes of responding to the Internal Revenue Service income tax audit, Form 1040, for the years 1988 and 1989.

Notes, workpapers, correspondence, memorandum and copies of or original records of KCS Industries Inc., furnished for purposes of responding to the Internal Revenue Service corporate income tax audit, Form 1120, for the years 1988 and 1989.

APPENDIX F — ATTACHMENT TO IRS SUMMONS, DATED JUNE 21, 1994

ATTACHMENT TO SUMMONS ISSUED TO: Richard A. Frederick

FOR THE YEARS: 1992

Any and all documents in your custody or control relative to the financial transactions of: Randolph W. Lenz

Including but not limited to the following:

All books, records, bank statements, canceled checks, deposit tickets, work-papers, financial statements, correspondence and other pertinent documents furnished by or on behalf of for the preparation of state and federal income tax returns and for any other entity in which either or both of them have a financial interest, including but not limited to:

All records used in or resulting from the preparation of federal and state income tax returns consisting of but not limited to work-papers, notes, papers, memoranda and correspondence used or prepared by you relative to the preparation of the aforementioned returns.

Copies of federal and state income and payroll tax returns, state sales tax returns and amended tax returns.

All records, books of account and other documents or papers relative to financial transactions of the principals.

All client billing records relative to this client to include records disclosing the dates and types of service rendered; client account cards; billing invoices; records reflecting the dates, amounts, purpose, and method of all payments (cash or check); and all correspondence with this client.

APPENDIX G — AFFIDAVIT OF RICHARD A. FREDERICK, DATED MAY 26, 1995

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WISCONSIN

Civil Action No. 94-C-1281

UNITED STATES OF AMERICA,

Petitioner,

– against –

RICHARD A. FREDERICK,

Respondent,

– and –

RANDOLPH W. LENZ, KARIN LENZ, and KCS INDUSTRIES, INC.,

Respondent-Intervenors.

AFFIDAVIT OF RICHARD A. FREDERICK IN OPPOSITION TO THE GOVERNMENT'S MOTION TO SUMMARILY ENFORCE TWO IRS SUMMONSES

STATE OF WISCONSIN)
: ss.:
COUNTY OF MILWAUKEE)

RICHARD A. FREDERICK, being duly sworn, deposes and says:

Appendix G

1. I am a member of the bar of this Court and the Respondent in the above entitled action.

2. I submit this affidavit in opposition to the United States' Motion to Summarily Enforce Two IRS Summonses and in support of the Joint Memorandum Of Law Of The Respondent and Respondent-Intervenors In Opposition To The Government's Motion To Summarily Enforce Two IRS Summonses.

3. I am a tax attorney in private practice in Milwaukee, Wisconsin. My offices are located at 1840 North Farwell Avenue, Suite 301, Milwaukee, Wisconsin. I provide tax advice to both corporations and individuals, assess the tax consequences of real estate and corporate transactions, represent clients in IRS examinations and audits, litigate on their behalf before the United States Tax Court and other federal courts, and prepare tax returns for clients I represent in other matters. I also represent clients in real estate and corporate transactions and occasionally litigate on their behalf against private parties.

Representation of the Lenzes and Related Companies

4. For over 15 years, I have acted as an attorney and represented the Lenzes and entities associated with them in a variety of capacities. Primarily, I have been retained by the Lenzes, KCS Industries, Inc. ("KCS"), Terex Corporation ("Terex"), Corsta Yacht Charters, Inc. ("Corsta Yacht"), Corsta Corp., FWD Corp. ("FWD"), Seagrave Racing, Inc. ("Seagrave Racing"), Alass Investment Partners, Ltd. ("Alass"), and Network Investment Real Estate Corp.

("Network") in the audits of their respective and related returns. I also have provided tax planning advice to the Lenzes and their children, as well as to several Lenz-related entities. I have represented the Lenzes and some Lenz-related entities in real estate and corporate transactions and in lawsuits against private parties. I have also been mindful of the pending criminal investigation and have consulted with Mr. Lenz's criminal counsel with respect to its implications.

5. During my representation of the Lenzes, I have become familiar with Mr. Lenz's businesses. On his tax return, Mr. Lenz lists his occupations as an industrialist. He specializes in turning around financially troubled organizations. To that end, Mr. Lenz has a number of business ventures operating concurrently. He currently is the Chairman of the Board of Directors of the Terex, a manufacturer of heavy duty construction equipment and trucks. Until recently, he was Chairman and Chief Executive Officer of KCS, a management services company. In addition, Mr. Lenz has interests in FWD, a fire equipment manufacturer; Corsta Corp., an investment company; Alass, an investment limited partnership; Seagrave Racing, a vintage race car investment firm; and Corsta Yacht, a yacht chartering company. In the past, Mr. Lenz invested in several real estate development concerns, including Network, Westwood Properties ("Westwood"), Equity Builders, Inc. ("Equity") and American Realty, Inc. Mr. Lenz currently invests in a variety of publicly-traded investment vehicles.

6. The Lenzes first retained me in the early 1980's. Having been notified that their 1976, 1977, 1978 and 1979 returns were under audit, the Lenzes were then concerned

about possible civil tax liability. They retained me to represent them before the IRS in these audits. I eventually settled these audits on very favorable terms.

7. Every year since they first retained me the IRS has at least audited a personal Lenz return or one of a business entity associated with Mr. Lenz. I have represented the Lenzes in the following IRS audits:

Lenzes' personal returns for 1976-1981 and 1984 to the present

Network's 1977-1981 returns

Corsta Yacht's 1984-1991 returns

Seagrave Racing's returns for 1989, 1990, 1991

KCS' returns for 1988-1992

Corsta Corp.'s returns for 1989-1990

FWD's returns for 1988-1990

Terex's returns for 1988-1992.

Three separate audits resulted in Tax Court litigations: the 1984 Lenz personal return; the 1986 and 1987 Lenz personal and Corsta Yacht returns and the 1988 Lenz personal return.

8. With this audit history, the Lenzes since the early 1980's have expected that every return they would file would be audited.

Appendix G

9. The IRS examined the same general type of issues year after year. Regardless of which entities' returns were audited, the following five recurring issues arose:

- The first issue was the proprietary of deductions of trade or business expenses. Mr. Lenz was, and is, involved in numerous business ventures and investments. Some were profitable; some were not. Losses sustained by these business ventures were properly deducted on various returns as trade or business expenses.

- The second issue, deductions for non-performing loans, is closely related to the first. Once in awhile, looking to make a profit, Mr. Lenz, or one of his companies, lent money to businesses that ultimately became insolvent. The losses Mr. Lenz or one of his companies sustained as a result often was deducted in one form or another, and the IRS repeatedly challenged them. This issue was one of the primary questions involved in the Tax Court litigation of Lenzes' 1984 return. The litigation concerned loans Mr. Lenz made to several real estate development corporations. The case turned on whether or not the loans were related to Mr. Lenz's business interests; the litigation was eventually settled by allowing a deduction equal to 70% of the unrecoverable debt. Closely related to this issue, deductions of worthless investments in the stock market and elsewhere also were frequently examined. Most every deduction for a worthless investment, whether by the Lenzes or a related entity, was questioned.

Appendix G

- The third recurring issue in these audits was investment interest expense. Mr. Lenz borrowed funds, in one form or another, to invest in his many ventures. The costs of this borrowing were deducted as investment interest expense on his personal returns. Investment interest expense was an issue in the 1986 and 1987 Tax Court litigations, as well as in the audits of KCS' 1989, 1990 and 1991 returns. The Tax Court ruled in the Lenzes' favor on the investment interest issue, and the Lenzes also prevailed in the Eleventh Circuit after the Government appealed the Tax Court ruling.

- The fourth repeating audit issue relates to items claimed as business expenses. In general, the IRS questioned certain business expenses deducted on the returns of Lenz-related entities. Over the years, this issue has appeared in many facets. For example, the IRS mistakenly believed that Mr. Lenz or his family personally used a few of the assets owned by entities associated with Mr. Lenz. In the audits of Corsta Yacht and in the Tax Court litigation associated with the 1986 and 1987 Corsta Yacht returns, the IRS claimed that certain business expense deductions were personal expenses of Mr. Lenz. The Tax Court litigation was eventually settled on a 50-50 basis. Somewhat related to this fourth audit issue was the IRS' questioning of travel and expense deductions relating to Mr. Lenz by one of his companies. For example, the IRS questioned KCS's payment of legal fees, including mine for representing KCS in the audits of its returns, claiming that they related to the

personal business of Mr. Lenz. This question was an issue in the audit of KCS' 1988 return and is a matter now before the Tax Court in the litigation pertaining to the Lenzes' 1988 return.

- The final recurring issue pertains to KCS and the Lenzes for the tax years 1989 and later. In 1989, through a complicated transaction, Terex acquired the Fruehauf Corporation. Mr. Lenz, KCS, and several other individuals and partnerships participated in the multi-level financing. The IRS has questioned various aspects of this transaction as they pertained to the returns of both the Lenzes and KCS for the 1989, 1990 and 1991 tax years.

10. As part of this representation, the Lenzes directed me to prepare their income tax returns, which I have done since 1981 to the present. In conjunction with the preparation of their returns I would advise the Lenzes and the entities associated with them about how reporting positions taken on their returns would affect or be affected by past, current and future tax audits and tax litigation relating to the Lenzes and the entities associated with them. Given the interrelationship of Mr. Lenz's investments, an audit of an entity in which he had an interest often impacted on issues associated with his personal return. Oftentimes, a particular return precipitated more than one audit. For example, Terex Corporation's return was often audited, and during the course of that audit, the Lenzes' personal return would be separately audited. *See, e.g.*, Terex IDR No. T-2, a true and correct copy of which is attached as Exhibit 1 to this Affidavit.

Appendix G

11. From the beginning, my preparation of the Lenzes' personal returns was part and parcel of my representation of them, and the closely-held entities they owned, in these recurring audits. Information I received from the Lenzes could not be neatly segregated into that legally analyzed for representations in audits and Tax Court litigation and that intended solely for the preparation of a return. In general, I assessed all information to measure the effect, if any, it might have in existing audits or pending Tax Court litigation. I also assessed varying treatments for certain information to determine how certain information would fair in the almost certain event of an audit. The Lenzes expected me to conduct these interrelated analyzes and expected that whatever information I deemed to remain confidential would not be disclosed.

Production Pursuant To The First Summons

12. My secretary, ostensibly on my behalf, was served with the first summons on or about February 4, 1993. By mutual agreement, I appeared before the IRS on June 8, 1993 and produced a total of 5,690 pages of records responsive to the summons. I also submitted to an interview with Special Agent James Hill that was not transcribed.

13. At this interview, I responded to most of Mr. Hill's questions, refusing to answer some of the questions on the grounds that the question called for information protected by either the attorney-client privilege or work product doctrine, or both, as the case may have been. I had been instructed by the Lenzes and all Lenz-related entities I have represented, to assert all applicable privileges.

14. On October 1, 1993, I provided additional records and a privilege log. The privilege log identified the documents that I withheld from production at the direction of either or both of the Respondent-Intervenors on the grounds that they were covered either by the attorney-client privilege or work product doctrine, or both, as the case may be. On December 1, 1993, I provided a supplemental privilege log referencing additional records withheld from production at the direction of either or both of the Respondent-Intervenors due to the existence of either or both of the aforementioned privileges, as the case may be.

15. A total of 806 pages of documents were withheld pursuant to the attorney-client privilege and/or the work product doctrine. In addition, I, at the direction of one or both of the Respondent-Intervenors, redacted portions of 14 pages of documents on the grounds that the deleted information was non-responsive or was covered by the attorney-client privilege or work product doctrine, as the case may be.

Production Pursuant To The Second Summons

16. On November 16, 1994, the government filed its Petition to enforce both summonses. On December 7, 1994, I produced 811 pages of documents in response to the second summons. I also provided a Privilege Log, which detailed, document-by-document, the documents I, at the direction of and on behalf of my clients, withheld from production due to the attorney-client privilege and work product doctrine. (The Privilege Log is attached as Exhibit A to the Answer of Richard A. Frederick ("Frederick Answer").) In addition,

Appendix G

I redacted six documents. (The Redaction Log is attached as Exhibit B to the Frederick Answer.) I had previously thought from my conversations and correspondence with the IRS Special Agents that they had afforded me additional time to comply with this summons, an impression I realized was mistaken when the government filed this enforcement action.

Particular Document Analysis

17. The documents withheld from both summonses fall into the following five general categories:

Draft Returns and Other Tax Forms: FPR-415-417; FPR-418-423; FPR-424-432; FPR-433-443; FPR-444-468; FPR-469; FPR-470-483; FPR-494; FPR-497-498; FPR-499-500; FPR-502-508; FPR-509-526; FPR-527-528; FPR-529-534; FPR-542-567; FPR-568-602; FPR-603-616; FPR-100000-100036

Draft Worksheets: FPR-487; FPR-490; FPR-491; FPR-492; FPR-493; FPR-501; FPR-535; FPR-536; FPR-537; FPR-618; FPR-100038-100068; FPR-100069-100071; FPR-100072-FPR-100073; FPR-100074-100097; FPR-100098-100110; FPR-100111-100122; FPR-100128; FPR-100197-100215; FPR-100217-100225

Handwritten Notes: FPR-414; FPR-484; FPR-485; FPR-486; FPR-538-539; FPR-540; FPR-541; FPR-100127; FPR-100130; FPR-100131

Appendix G

Letters and Faxes: FPR-488-489; FPR-415-417; FPR-495-496; FPR-100129; FPR-100216; FPR-100134-100136; FPR-100228; FPR-100229

Memoranda To File: FPR-100037; FPR-100180-100193; FPR-100194-100195;

Draft Returns And Other Tax Forms

18. I prepared all of the draft tax returns, other tax forms, worksheets, and notes withheld. Most of the withheld documents are preliminary, incomplete, or completed for a purpose other than preparing an entire return. I also prepared some of the letters and faxes withheld, and the memoranda in question were either prepared by me or at my direction. They all reflect confidential communications between the Lenzes and me, and some were prepared in anticipation of litigation. Each document withheld is described in the Document Inventory previously filed with the Court. In the Appendix to this Affidavit, I now provide additional information, filed under seal, on a document-by-document basis. This information is filed under seal because it reflects privileged matters.

s/ Richard A. Frederick
Richard A. Frederick

Sworn to before me this
26th day of May, 1995

s/ Susan J. Seymour
Notary Public
My commission expires 3/1/98.

APPENDIX H — FIRST SUPPLEMENTAL AFFIDAVIT OF RICHARD A. FREDERICK, DATED JUNE 21, 1995 WITH ATTACHMENT A

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WISCONSIN

Civil Action No. 94-C-1281

UNITED STATES OF AMERICA,

Petitioner,

v.

RICHARD A. FREDERICK,

Respondent,

and

RANDOLPH W. LENZ, KARIN LENZ, and KCS INDUSTRIES,

Respondent-Intervenors

FIRST SUPPLEMENTAL AFFIDAVIT OF RICHARD A. FREDERICK

State of Wisconsin)
) ss.
Milwaukee County)

RICHARD A. FREDERICK, being first duly sworn on oath, deposes and states as follows:

Appendix H

1. That I make this Affidavit for the purpose of responding to the Petitioner's United States of America's Response to Joint Memorandum of Law of Respondent and Respondent-Intervenors and the Second Supplemental Declaration of IRS Special Agent James A. Hill included therein.

2. That notwithstanding Mr. Hill's "review of the IRS records" which indicated to him that I did not represent the Lenzes in the Terex audit, attached hereto as Exhibit A is a copy of a letter I sent to Pamela Prevost, a revenue agent of the IRS, advising her that I represented Mr. Lenz in connection with the Terex Corporation audit, which at that time encompassed matters affecting tax years 1987 through 1990. The letter is redacted in part to protect the privacy of the matters set forth therein.

3. That the following documents have already been produced to the IRS:

   a) P-3299 – Form 4868 — Application for Automatic Extension of Time to File U.S. Individual Income Tax Return for 1990 filed by Mr. and Mrs. Lenz on April 15, 1991;

   b) P-3300 — check payable to the IRS from Mr. and Mrs. Lenz for $362,802 dated April 15, 1991; and

   c) P-3301 — proof of mailing of P-3300 and P-3299.

4. That documents P-3299, P-3300 and P-3301 demonstrate that the reason for the change in tax liability from that

indicated in the letter from me to Mr. Lenz dated April 15, 1991, which letter is referred to in paragraph 1 of James A. Hill's Second Supplemental Declaration, and the tax return which was filed, was due in part to a $362,802 deposit of estimated tax on April 15, 1991 made by the Lenzes, rather than because of a "dramatic variation in the Lenz's reported income" as suggested in paragraph 3 of Mr. Hill's Second Supplemental Declaration.

s/ Richard A. Frederick
Richard A. Frederick

Dated this 21st day of June, 1995

s/ Trudy M. Miller
Notary Public, STATE OF WISCONSIN
My Commission 7/5/95

Appendix H

EXHIBIT A

RICHARD A. FREDERICK
Attorney at Law

1840 NORTH FARWELL AVENUE • SUITE 301
MILWAUKEE, WISCONSIN 53202
TELEPHONE (414) 271-7779

November 5, 1991

Ms. Pamela Prevost
Internal Revenue Service
1216 West Wisconsin Avenue
Appleton, WI 54914

Re: Randolph W. and Karin Lenz
SS#: 388-48-2573 and 391-56-0917

Dear Ms. Prevost:

Under dates of July 16 and July 29, 1991 you had provided Terex Corporation with Information Document Requests (Form 4564), Requests Numbered T-2 and T-10, requesting, among other things, certain information relating to Messrs. Randolph W. Lenz, the Chairman of the Board respectively, of Terex Corporation. I have been asked by Mr. Lenz to provide certain of the information directly to you. I am enclosing Powers of Attorney from Mr. and Mrs. Lenz for 1988 and 1989 permitting me to represent them in these proceedings. I shall forward a 1990 Power of Attorney to you upon receipt.

Appendix H

Mr. Lenz expects that the information provided herein remain confidential in accordance with Internal Revenue Code Regulations notwithstanding that the taxpayer is related to Terex Corporation.

Sincerely yours,

s/ Richard A. Frederick
RICHARD A. FREDERICK

RAF/ss
Enclosures
cc: Mr. Randolph W. Lenz

APPENDIX I — DECLARATION OF IRS SPECIAL AGENT JAMES A. HILL, DATED OCTOBER 20, 1994

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WISCONSIN

Civil Action No. 94-C-1281

UNITED STATES OF AMERICA,

Petitioner,

v.

RICHARD A. FREDERICK,

Respondent.

DECLARATION OF IRS SPECIAL AGENT JAMES A. HILL

1. I am a duly commissioned Special Agent of the Internal Revenue Service; I am employed in the Criminal Investigation Division of the Office of the District Director at Green Bay, Wisconsin.

2. I am conducting an investigation into the federal tax liabilities of Randolph W. Lenz for the years 1988, 1989, 1990, 1991, and 1992. This investigation is being conducted jointly with the Examination Division of the IRS, which seeks to determine the extent and nature of Lenz's civil tax liabilities.

3. As part of the investigation described in paragraph 2, and pursuant to the authority granted in 26 U.S.C. Section 7602(a), IRS Special Agent Thomas C. Glunz issued an administrative summons ("the first summons") to Richard A. Frederick ("Frederick") on February 4, 1993. A copy of the first summons is attached hereto as Exhibit A. Special Agent Glunz has informed me that on February 4, 1993, he served the first summons on Frederick by handing an attested copy to Susan Seymour, Frederick's secretary. The manner in which the first summons was served, is set forth in the memorandum of Special Agent Glunz, which is attached hereto as Exhibit B.

4. The first summons directed Frederick to appear before me at the IRS offices, located at 310 W. Wisconsin Avenue, Milwaukee, Wisconsin, on March 2, 1993, to testify and to produce for examination certain documents and records, which are identified on the summons, and which relate to Randolph W. Lenz's federal tax liabilities for the years 1988, 1989, 1990, and 1991.

5. On February 4, 1993, Special Agent Glunz served notice of the first summons on Randolph W. Lenz and Karin Lenz, and KCS Industries, Inc., by certified mail, in accordance with 26 U.S.C. Section 7609(a). *See* Exhibit A.

6. By mutual agreement, the appearance date of March 2, 1993, was extended to June 8, 1993, on which date Frederick appeared at the IRS offices in Waukesha, Wisconsin, with two boxes of records.

7. At a meeting with agents of the IRS in Waukesha on June 8, 1993, Frederick was asked questions about his

responsibilities and duties as the preparer of Randolph W. Lenz's personal income tax returns and his role as taxpayer's representative during the corporate income tax audit of KCS Industries, Inc., for the years 1988 and 1989. In response to many of these questions, Frederick refused to answer on the grounds of attorney-client privilege.

8. On October 1, 1993, Frederick provided additional records, a privilege log that references documents not provided, and a redaction log that references deletions from records. Copies of the privilege log and the redaction log are attached hereto as Exhibits C and D, respectively.

9. On December 1, 1993, Frederick provided a supplemental privilege log referencing additional records not provided. A copy of the supplemental privilege log is attached hereto as Exhibit E.

10. Frederick furnished a total of 5,690 pages of records, including work papers, schedules, stock account records, IRS Forms W-2, receipts, correspondence, records relating to the IRS audit of KCS industries for the years 1988 and 1989, and copies of completed IRS Forms 1040 for Randolph W. and Karin Lenz.

11. A total of 806 pages of records were not furnished, pursuant to the attorney-client privilege and/or the work product privilege. Deletions were made on 14 pages of documents on the grounds that the deleted information was non-responsive, or pursuant to the attorney-client privilege and/or the work product privilege.

12. The books, papers, records, or other data sought through the first summons have been furnished and are in the possession of the IRS, with the exception of the 806 pages of documents shown on Exhibits C and E, and the deletions to 14 pages of documents shown on Exhibit D.

13. It is necessary to obtain Frederick's testimony and to examine the remainder of the records not furnished in order to properly investigate the federal tax liabilities of Randolph W. Lenz for the years 1988, 1989, 1990, and 1991.

14. As part of the investigation described in paragraph 2, and pursuant to the authority granted in 26 U.S.C. Section 7602(a), I issued another administrative summons ("the second summons") to Frederick on June 21, 1994. A copy of the second summons is attached hereto as Exhibit F. On June 22, 1994, I served the second summons on Frederick by handing an attested copy to him.

15. The second summons directed Frederick to appear before me at the IRS offices, located at 1920 Libal Street, Green Bay, Wisconsin, on July 18, 1994, to testify and to produce for examination certain documents and records, which are identified on the summons, and which relate to Randolph W. Lenz's federal tax liabilities for the year 1992.

16. On June 23, 1994, I served notice of the second summons on Randolph W. Lenz, by certified mail, in accordance with 26 U.S.C. Section 7609(a).

17. I extended the date for production of documents requested in the second summons to August 18, 1994.

Frederick did not appear in response to the second summons on August 18, 1994, and has not produced the requested documents since that time.

18. It is necessary to obtain Frederick's testimony and to examine the records requested in the second summons in order to properly investigate the federal tax liabilities of Randolph W. Lenz for the year 1992.

19. With respect to both summonses described above, all administrative steps required by the IRS for issuance of a summons have been taken.

20. There has been no criminal referral to the United States Department of Justice within the meaning of 26 U.S.C. Section 7602(c)(2).

Pursuant to 28 U.S.C. Section 1746, I declare under penalty of perjury that the foregoing is true and correct.

Executed on October 20, 1994.

s/ James A. Hill
JAMES A. HILL

(2)

No. 99-719

Supreme Court, U.S.
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In The

Supreme Court of the United States

RICHARD A. FREDERICK, RANDOLPH W. LENZ, KARIN LENZ AND KCS INDUSTRIES, INC.,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

BRIEF OF AMICUS CURIAE AMERICAN ASSOCIATION OF ATTORNEY-CERTIFIED PUBLIC ACCOUNTANTS, INC. IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

L. HAROLD LEVINSON*
Vanderbilt University Law School
131 21st Avenue South
Nashville, TN 37203
(615) 322-2540

PHILIP D. BRENT
PHILIP D. BRENT, PROFESSIONAL CORPORATION
15915 Ventura Blvd., Suite 203
Encino, CA 91436
(818) 990-2444

Attorneys for Amicus Curiae, American Association of Attorney-Certified Public Accountants, Inc.

**Counsel of Record*

[Additional Counsel Listed On Inside Cover]

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

168

Silvia S. Ibanez
Silvia S. Ibanez Law Office
3956 Town Center Blvd.
Suite 196
Orlando, FL 32837
(407) 856-9449

Thomas W. McCulloch
Thomas W. McCulloch, LLC
2810 Summit Tower
Eleven Greenway Plaza
Houston, TX 77046
(713) 961-1099

David Ostrove
Ostrove, Krantz & Ostrove
A Professional Corporation
5757 Wilshire Blvd.
Suite 535
Los Angeles, CA 90036
(323) 939-3400

C. Murray Saylor, Jr.
The Saylor Law Firm LLP
100 Colony Square
Suite 1224
1175 Peachtree Street, N.E.
Atlanta, GA 30361
404/892-4400

Sydney S. Traum
Sydney S. Traum, P.A.
Zack Kosnitzky, P.A.
100 S.E. 2nd Street
Suite 2800
Miami, FL 33131
(305) 539-8400

TABLE OF CONTENTS

Page

Table of Authorities iii

Consent of the Parties 1

Interest of Amicus Curiae 1

Summary of Argument 2

Argument 2

I. The Court of Appeals erred in denying the attorney-client and work product privileges to "accountant's work" performed by a lawyer ... 2

A. The Court of Appeals' distinction between "accountant's work" and "lawyer's work" is inappropriate and unnecessary 3

1. The court's distinction is inappropriate... 4

2. The court's distinction is unnecessary.. 5

B. The Court of Appeals improperly considered competition between lawyers and accountants as a factor in its denial of the privileges to "accountant's work" performed by a lawyer 5

C. The Court of Appeals' decision needlessly complicates the practice of law and discourages candid communications between lawyers and clients 6

D. The Court of Appeals' decision may discourage lawyers from acquiring or using knowledge or skills in non-law areas 7

TABLE OF CONTENTS – Continued

Page

II. The Court of Appeals should have applied the privileges to all professional services performed by a lawyer for a client, without regard to whether similar types of services may also be performed by non-lawyers 8

A. The approach proposed in this brief is consistent with the common law 8

B. The approach proposed in this brief protects the reasonable expectations of clients and will encourage candid communication between lawyers and clients 10

C. The approach proposed in this brief protects the interests of the government and other parties seeking access to information 11

D. The approach proposed in this brief promotes the public interest in the broad education of lawyers and in their appropriate use of non-law knowledge and skills for the benefit of clients 12

Conclusion 12

TABLE OF AUTHORITIES

Page

CASES:

Colton v. United States, 306 F.2d 633 (2d Cir. 1962), *cert. denied*, 371 U.S. 951 (1963) 4

United States v. Abrahams, 905 F.2d 1276 (9th Cir. 1990) 4

United States v. Kovel, 296 F.2d 918 (2d Cir. 1961) 4

RULES:

Internal Revenue Service, Rules of Practice, 31 CFR Part 10 (1998) 11

Internal Revenue Service, Rules of Practice, 31 CFR § 10.29 (1998) 11

OTHER AUTHORITIES:

Restatement of the Law Governing Lawyers, Proposed Final Draft No. 1 (March 29, 1996) ... 8, 10, 11

C. Murray Saylor, Jr., *Privilege and Tax Return Preparation*, 35 The Attorney-CPA, No. 2 (1999) at 7. 4

Charles W. Wolfram, Modern Legal Ethics (1986) ... 10, 11

CONSENT OF THE PARTIES

All parties have consented to the participation of the American Association of Attorney-Certified Public Accountants, Inc. in these proceedings as amicus curiae in support of the petition for writ of certiorari. Their consents have been filed with this Court.[1]

INTEREST OF AMICUS CURIAE

The American Association of Attorney-Certified Public Accountants, Inc. ("AAA-CPA" or "the Association") is a not-for-profit corporation, formed in 1964 and now headquartered in California, with members located all over the United States. Every member has been licensed as both an attorney and a certified public accountant.

AAA-CPA is dedicated to ensuring that its members observe the highest professional and ethical standards in service to their clients and the public. At the same time, AAA-CPA supports the right of practitioners to disclose truthful information about their qualifications, and to engage in the practice of either or both of their professions. The Association has filed amicus curiae briefs in other cases before this Court involving the regulation of individuals who are licensed in one or more professions.

AAA-CPA is in a unique position to evaluate the distinction made by the Court of Appeals for the Seventh

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[1] None of the counsel for the parties authored this brief in whole or in part. No person or entity, other than the amicus curiae, its members or its counsel, made any monetary contribution to the preparation or submission of this brief.

Circuit in this case, between "lawyer's work" (to which the court applies the attorney-client and work product privileges) and "accountant's work" (to which the court does not apply the privileges even when this work is performed by a lawyer).

In this brief, AAA-CPA respectfully submits to this Court a proposed approach to the resolution of this case. The Association supports the petitioners in their request for writ of certiorari.

SUMMARY OF ARGUMENT

I. THE COURT OF APPEALS ERRED IN DENYING THE ATTORNEY-CLIENT AND WORK PRODUCT PRIVILEGES TO "ACCOUNTANT'S WORK" PERFORMED BY A LAWYER.

II. THE COURT OF APPEALS SHOULD HAVE APPLIED THE PRIVILEGES TO ALL PROFESSIONAL SERVICES PERFORMED BY A LAWYER FOR A CLIENT, WITHOUT REGARD TO WHETHER SIMILAR TYPES OF SERVICES MAY ALSO BE PERFORMED BY NON-LAWYERS.

ARGUMENT

I. The Court of Appeals erred in denying the attorney-client and work product privileges to "accountant's work" performed by a lawyer

The Court of Appeals applied the attorney-client and work product privileges to "lawyer's work," but not to

"accountant's work" even when the "accountant's work" is performed by a lawyer.

A. The Court of Appeals' distinction between "accountant's work" and "lawyer's work" is inappropriate and unnecessary

The court did not define "accountant's work," but the court's opinion implies the term means the type of service customarily performed by acccuntants. The court denied the privileges to the following types of "accountant's work," even when performed by a lawyer:

> preparation of tax returns and related worksheets;
>
> preparation of draft tax returns and related worksheets;
>
> "dual-purpose documents" prepared for use both in tax returns and in litigation with the Internal Revenue Service ("IRS") – the court indicated that the unprivileged nature of the "accountant's work" of preparing tax returns destroys the privileges which would otherwise apply to the "lawyer's work" of preparing for litigation.

In addition, the court used the concept of "accountant's work" to deny the privileges to some types of documents prepared in connection with IRS audits of tax returns. In this category, the court characterized documents as "accountant's work" (and therefore unprivileged) if prepared merely to verify the accuracy of the return. In contrast, the court characterized documents as "lawyer's work" (and therefore privileged) if prepared

to enable the lawyer to deal with areas of statutory interpretation or case law that the revenue agent may have raised during the audit of a tax return.

1. The court's distinction is inappropriate

The court's distinction between "accountant's work" and "lawyer's work" is inappropriate for the following reasons:

First, the court does not offer any information or authority to support this distinction, which conflicts with precedents of other circuits, such as *United States v. Abrahams*, 905 F.2d 1276, 1284 (9th Cir. 1990); *Colton v. United States*, 306 F.2d 633, 637 (2d Cir. 1962), *cert. denied*, 371 U.S. 951 (1963); *United States v. Kovel*, 296 F.2d 918, 922-23 (2d Cir. 1961). The court does not mention these precedents, nor does the court explain the need to reject them. Further, the court does not address the related theory that tax return preparation may be the practice of law, even though non-lawyers are allowed to perform it. This theory notes that tax preparation necessarily requires interpretation of the tax laws as applied to the taxpayer's facts. Interpretation of statutes is an integral part of the practice of law. The interpretation of the tax law, together with reporting to the IRS and defending what has been reported, is given special prominence in legal education at the J.D. and LL.M. levels, in bar examinations, and in continuing legal education programs. *See* C. Murray Saylor, Jr., *Privilege and Tax Return Preparation*, 35 The Attorney-CPA, No. 2 (1999) at 7.

Second, the court fails to recognize the significant overlap between the services customarily performed by accountants and by lawyers. In practice, many tax returns are prepared by accountants, while others are prepared by lawyers, still others are prepared by teams including members of each profession, and some are prepared by individuals who are neither lawyers nor accountants. The preparation of tax returns, therefore, is not the exclusive province of either profession.

2. The court's distinction is unnecessary

The court's distinction between "accountant's work" and "lawyer's work" is unnecessary to the decision of this case. As suggested later in this brief, the crucial issue is whether the clients retained the lawyer to render professional services in a lawyer-client relationship. The proper resolution of this issue does not depend on whether non-lawyers may also render similar services to their clients.

B. The Court of Appeals improperly considered competition between lawyers and accountants as a factor in its denial of the privileges to "accountant's work" performed by a lawyer

The court based its decision, in substantial part, on the proposition that lawyers would receive an inappropriate competitive advantage over accountants if the privileges applied to "accountant's work" when performed by lawyers. The court offered no support for this proposition.

The issue of inter-professional competition is complex, and involves comparisons based on such factors as type of service, expertise, regulatory regime, and public perceptions. Without a comprehensive study of all relevant factors, the court acted improperly by basing its decision, in part, on its unexplained perception of the impact of its decision on competition between accountants and lawyers.

C. The Court of Appeals' decision needlessly complicates the practice of law and discourages candid communications between lawyers and clients

The court's decision, if allowed to stand, will create a precedent which needlessly complicates the practice of law. Lawyers in tax practice will have to do their best to distinguish unprivileged "accountant's work" from privileged "lawyer's work." On the basis of this distinction, lawyers will be well advised to inform clients of the limitations of the privileges, to place limits on communications with clients, and to consider adopting special records retention systems regarding unprivileged material.

The precedent will, in addition, affect virtually all lawyers, since it is almost inevitable that a lawyer has some type of knowledge or skills beyond the traditional scope of the law. Lawyers generally acquire extensive non-law knowledge and skills during their undergraduate studies before law school. Many law school courses include coverage of non-law disciplines, as do many continuing legal education programs. Many lawyers possess

non-law knowledge and skills in areas such as foreign languages, engineering, literature, medicine, investments, accounting and economics.

The court's decision threatens to destroy the privileges whenever a lawyer uses non-law knowledge and skills while serving in an attorney-client relationship.

D. The Court of Appeals' decision may discourage lawyers from acquiring or using knowledge or skills in non-law areas

Lawyers may reduce their attempts to acquire non-law knowledge and skills, if their use of such knowledge or skills in the practice of law will result in loss of the lawyer-client and work product privileges. This result would be contrary to the public interest in a broadly educated legal profession.

Further, lawyers may be discouraged from using their existing non-law knowledge and skills in the representation of clients, if this use would destroy the privileges. This result would be contrary to the interest of clients in many areas of practice in which non-law knowledge and skills may be useful, such as tax, patent, copyright, domestic relations, commercial law, professional liability, and many other areas of practice.

II. The Court of Appeals should have applied the privileges to all professional services performed by a lawyer for a client, without regard to whether similar types of services may also be performed by non-lawyers

Instead of basing its decision on the difference between "accountant's work" and "lawyer's work," the court should have applied the privileges to all professional services performed by a lawyer for a client, without regard to whether similar types of services may also be performed by non-lawyers.

A. The approach proposed in this brief is consistent with the common law

The approach suggested here is consistent with the common law, as reflected in the Restatement of the Law Governing Lawyers, Proposed Final Draft No. 1 (March 29, 1996) ("Restatement"). The Restatement deals with the situation where "a lawyer's services are of a kind performed commonly by both lawyers and non-lawyers or that otherwise include both legal and non-legal elements." § 122, cmt. c. This comment concludes:

> So long as the client consults to gain advantage from the lawyer's legal skills and training, the communication is within this Section [and therefore privileged], even if the client may expect to gain other benefits as well, such as business advice or the comfort of friendship. The primary consideration is the reasonable expectations of the person in the position of the putative client.

The same comment offers two illustrations of this principle in the context of tax practice. In the first, the

lawyer prepares a client's tax return which is not complex, and does not require a knowledge of tax law beyond that possessed by non-lawyer tax preparers. Neither the client nor the lawyer discusses any legal questions. The lawyer charges a fee comparable to the amount charged by non-lawyer tax preparers. In this situation, "[t]he trier of fact may, but need not, infer that the Client's purpose was not that of obtaining legal assistance." The Reporter's Notes to this illustration observe that "The decisions disagree whether routine tax-return preparation services constitute legal services covered by the privilege."

In the next illustration in the Restatement:

> Client has frequently consulted Lawyer about legal matters relating to Client's growing business. Lawyer drafts documents and provides other legal assistance relating to a complicated transaction having important tax implications that Client and Lawyer identify and discuss. Client later asks Lawyer to prepare Client's tax return for the year in which the transaction occurs. The circumstances indicate that Lawyer is providing legal services in preparing the tax return.

These illustrations suggest there is a continuum of tax services, ranging from the preparation of routine returns to tax services in more complex settings. The degree of complexity does not, of itself, determine whether preparation of the return is "lawyer's work" or not. Rather, the degree of complexity indicates the expectation of the client when obtaining the service. The more complex the situation, the more likely it is that the client expects to enter into an attorney-client relationship with the lawyer who performs the services. The facts of the

instant case indicate clearly that the petitioner clients retained the petitioner lawyer because they wanted legal services in a complex combination of tax returns and IRS audits.

The approach suggested in this brief would not change the common-law exceptions to the privileges. For example, the scrivener's exception would still apply, Restatement § 122, cmt. c, because the client could not reasonably expect to enter into an attorney-client relationship if the lawyer merely acted as a public stenographer. Also, the exception for lawyers while functioning as corporate directors and officers would still apply, *see* Charles W. Wolfram, Modern Legal Ethics 739-40 (1986), because lawyers who perform these functions act in a separate role of director or officer, rather than as attorney for the corporate client. Therefore, the corporate client could not reasonably expect the attorney-client relationship to extend to the lawyer's performance of duties as director or officer.

B. The approach proposed in this brief protects the reasonable expectations of clients and will encourage candid communication between lawyers and clients

The approach suggested here protects the reasonable expectations of clients. When a client enters into an attorney-client relationship, the client may reasonably rely on the lawyer's knowledge and skill, and also on the regulatory system that governs the conduct of lawyers. That system, administered by the states, applies to lawyers in all types of practice, unless superseded by other law.

Thus a lawyer in federal tax practice is governed by the rules of professional conduct of the applicable state, as well as by the Internal Revenue Service ("IRS") Rules of Practice, 31 CFR Part 10 (1998), which govern tax practitioners in general. For example, the IRS rules prohibit conflicts of interest, but imply that all conflicts are waivable, 31 CFR § 10.29. In contrast, the lawyers' rules of professional conduct make some conflicts non-waivable; *see* Charles W. Wolfram, Modern Legal Ethics 341-43 (1986). A client who retains a lawyer for tax services may rely on the more comprehensive protection provided by the lawyers' rules of professional conduct. Similarly, this client should be able to rely on the privileges which have been traditionally associated with the attorney-client relationship. If the client cannot rely on these privileges, candid communication between lawyer and client may be chilled.

C. The approach proposed in this brief protects the interests of the government and other parties seeking access to information

The IRS and other parties who seek access to information are protected by the approach proposed in this brief. The IRS is protected by its ability, in appropriate cases, to issue subpoenas to the taxpayer, to decide factual issues adversely to the taxpayer for lack of evidence, and to invoke the crime-fraud exception to the attorney-client privilege, Restatement § 132, and to the work product privilege, Restatement § 142. Other parties who seek access to information have similar protection.

D. The approach proposed in this brief promotes the public interest in the broad education of lawyers and in their appropriate use of non-law knowledge and skills for the benefit of clients

The approach suggested in this brief allows lawyers to broaden their education by acquiring non-law knowledge and skills, and to use such knowledge and skills appropriately for the benefit of clients, without jeopardizing the attorney-client and work product privileges. The public interest is served by a broadly educated legal profession.

CONCLUSION

For the reasons stated above, this Court should grant the petition for writ of certiorari.

Respectfully submitted,

L. HAROLD LEVINSON *
Vanderbilt University Law School
131 21st Avenue South
Nashville, TN 37203
(615) 322-2540

* *Counsel of Record*

PHILIP D. BRENT
PHILIP D. BRENT, PROFESSIONAL CORPORATION
15915 Ventura Blvd., Suite 203
Encino, CA 91436
(818) 990-2444

SILVIA S. IBANEZ
SILVIA S. IBANEZ LAW OFFICE
3956 Town Center Blvd., Suite 196
Orlando, FL 32837
(407) 856-9449

THOMAS W. MCCULLOCH
THOMAS W. MCCULLOCH, LLC
2810 Summit Tower
Eleven Greenway Plaza
Houston, TX 77046
(713) 961-1099

DAVID OSTROVE
OSTROVE, KRANTZ & OSTROVE, A PROFESSIONAL CORPORATION
5757 Wilshire Blvd., Suite 535
Los Angeles, CA 90036
(323) 939-3400

C. MURRAY SAYLOR, JR.
THE SAYLOR LAW FIRM LLP
100 Colony Square, Suite 1224
1175 Peachtree Street, N.E.
Atlanta, GA 30361
(404) 892-4400

SYDNEY S. TRAUM
SYDNEY S. TRAUM, P.A.
ZACK KOSNITZKY, P.A.
100 S.E. 2nd Street, Suite 2800
Miami, FL 33131
(305) 539-8400

Attorneys for Amicus Curiae, American Association of Attorney-Certified Public Accountants, Inc.

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No. 99-719

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In the Supreme Court of the United States

RICHARD A. FREDERICK, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

SETH P. WAXMAN
Solicitor General
Counsel of Record

LORETTA C. ARGRETT
Assistant Attorney General

FRANK P. CIHLAR
ANNETTE M. WIETECHA
Attorneys

Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

14 pp

QUESTION PRESENTED

Whether accounting worksheets and related information prepared for tax returns and tax audits are protected from disclosure pursuant to an Internal Revenue Service summons by either the attorney-client privilege or the work-product doctrine.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	4
Conclusion	10

TABLE OF AUTHORITIES

Cases:

Binks Mf. Co. v. *National Presto Indus., Inc.*, 709 F.2d 1109 (7th Cir. 1983)	8
Canaday v. *United States*, 354 F.2d 849 (8th Cir. 1966)	5
Colton v. *United States*, 306 F.2d 633 (2d Cir. 1962), cert. denied, 371 U.S. 951 (1963)	6, 7
Couch v. *United States*, 409 U.S. 322 (1973)	5, 9
Fisher v. *United States*, 425 U.S. 391 (1976)	4
Grand Jury Investigation, In re, 842 F.2d 1223 (11th Cir. 1987)	5
Hickman v. *Taylor*, 329 U.S. 495 (1947)	4
Rogers v. *Lodge*, 458 U.S. 613 (1982)	10
Tiffany Fine Arts, Inc. v. *United States*, 469 U.S. 310 (1985)	10
United States v. *Abrahams*, 905 F.2d 1276 (9th Cir. 1990)	6, 7, 9
United States v. *Adlman*, 134 F.3d 1194 (2d Cir. 1998)	6, 7
United States v. *Arthur Young & Co.*, 465 U.S. 805 (1984)	5
United States v. *Bisceglia*, 420 U.S. 141 (1974)	4-5
United States v. *Bornstein*, 977 F.2d 112 (4th Cir. 1992)	5

Cases—Continued: Page

United States v. *Davis*, 636 F.2d 1028 (5th Cir.), cert. denied, 454 U.S. 862 (1981) 5
United States v. *El Paso Co.*, 682 F.2d 530 (5th Cir. 1982), cert. denied, 466 U.S. 944 (1984) 8
United States v. *Euge*, 444 U.S. 707 (1980) 4
United States v. *Gurtner*, 474 F.2d 297 (9th Cir. 1973) 5
United States v. *Laurins*, 857 F.2d 529 (9th Cir. 1988), cert. denied, 492 U.S. 906 (1989) 9-10
United States v. *Lawless*, 709 F.2d 485 (7th Cir. 1983) 5, 9
United States v. *Nobles*, 422 U.S. 225 (1975) 4
Upjohn v. *United States*, 449 U.S. 383 (1981) 4
Williams v. *Commissioner*, 1 F.3d 502 (7th Cir. 1993) 9

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BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-15a) is reported at 182 F.3d 496. The opinions of the district court (Pet. App. 16a-38a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on April 15, 1999, and amended on May 18, 1999. A petition for rehearing was denied on July 26, 1999 (Pet. App. 39a-40a). The petition for a writ of certiorari was filed on October 25, 1999 (a Monday). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner Richard Frederick is an attorney. He prepared the tax returns filed by petitioners Randolph and Karin Lenz and their company, KCS Industries, Inc. (Pet. App. 2a). In connection with an investigation of the Lenzes and their company, the Internal Revenue Service issued summonses to Frederick directing him to produce various documents—including tax forms and worksheets—relating to the preparation of these tax returns (*ibid.*). Although Frederick substantially complied with the summonses, he claimed that approximately 800 pages of documents were protected by the attorney-client privilege, the work-product doctrine, or both (*id.* at 17a). When the United States brought this suit to enforce the summonses, the Lenzes and their company intervened (*id.* at 2a, 33a).

2. The district court ordered the summonses enforced as to most of the tax forms and worksheets which it found contained "information reported to an accountant but not confidential communication between a client and attorney" (Pet. App. 36a). Noting that "potential inferences of confidential communication are not enough to warrant the privilege," the court held that petitioners failed to produce any evidence to establish that the documents in fact represented privileged communications (*id.* at 36a-37a). The court concluded that the work-product doctrine was also inapplicable to these documents, which reflected "accounting calculations but not legal theories" (*id.* at 37a). The court held that "draft returns and worksheets that do not contain written notations are not protected by the work product doctrine" (*ibid.*).

The court then conducted an *in camera* review of the remaining documents such as handwritten notes,

letters, facsimiles, memoranda, redacted documents and other draft returns (Pet. App. 34a, 38a). The court found that 16 of these documents were privileged as confidential attorney-client communications or attorney work-product (*id.* at 27a-28a). The court concluded that the remainder of the documents were not privileged. Some were not privileged because they were of a type that would be created by an accountant for preparation of the tax returns (*id.* at 20a-21a). With respect to some documents, the attorney-client privilege had been waived (*id.* at 22a). And, with respect to several documents, petitioners had not offered evidence to fulfill their burden of proof to sustain a privilege (*id.* at 23a-25a).

3. The court of appeals affirmed (Pet. App. 1a-15a). The court stated that the clearly erroneous standard of review applies to the mixed question of fact and law involved in determining "[w]hether a particular document is privileged" (Pet. App. 3a), and the court found no clear error in the findings of the district court.

The court observed that some of the contested documents were created both for use in preparing tax returns and for use in litigation (Pet. App. 4a-6a). The court held that this sort of "dual purpose" document must be disclosed because, "otherwise, people in or contemplating litigation would be able to invoke, in effect, an accountant's privilege, provided that they used their lawyer to fill out their tax returns" (*id.* at 8a).

The court similarly held that documents created in connection with audits of petitioners' tax returns were not protected by the work-product doctrine (Pet. App. 9a). The court noted that "an audit is both a stage in the determination of tax liability * * * and a possible antechamber to litigation" (*ibid.*). The court stated that the work-product doctrine may not be invoked to pro-

tect information prepared by an accountant to complete or "verify[] the accuracy of a return" because "this is accountants' work and it remains such even if the person rendering the assistance is a lawyer rather than an accountant" (*ibid.*). Although the privilege unquestionably applies when "the lawyer is doing lawyer's work," none of the contested documents related to that type of representation (*ibid.*).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. a. As this Court has noted, summonses are "subject to the traditional privileges and limitations." *United States* v. *Euge*, 444 U.S. 707, 714 (1980). See also *Upjohn* v. *United States*, 449 U.S. 383, 397 (1981). The attorney-client privilege and the work-product doctrine may therefore be invoked in summons enforcement proceedings. These evidentiary privileges, however, are limited by their very nature. The attorney-client privilege "has the effect of withholding relevant information from the factfinder, [and] it applies only where necessary to achieve its purpose. Accordingly, it protects only those disclosures—necessary to obtain informed legal advice—which might not have been made absent the privilege." *Fisher* v. *United States*, 425 U.S. 391, 403 (1976). The work-product doctrine similarly applies only to the extent that it is necessary to protect documents prepared in anticipation of litigation. See *United States* v. *Nobles*, 422 U.S. 225, 238 (1975); *Hickman* v. *Taylor*, 329 U.S. 495, 510-511 (1947).

Apart from these traditional privileges, other restrictions on the summons power do not exist "absent

unambiguous directions from Congress." *United States* v. *Bisceglia*, 420 U.S. 141, 150 (1974). In particular, "no confidential accountant-client privilege exists under federal law, and no state-created [accountant-client] privilege has been recognized in federal cases." *Couch* v. *United States*, 409 U.S. 322, 335 (1973). See also *United States* v. *Arthur Young & Co.*, 465 U.S. 805, 817-819 (1984).

b. Petitioners err in contending (Pet. 8-14) that "dual purpose" accounting documents—created for use both in preparation of a tax return and in assisting the attorney in giving legal advice—are protected by the attorney-client privilege or the work-product doctrine. Information intended "for use in connection with the preparation of tax returns" constitutes "an unprivileged category of numbers" (Pet. App. 8a). The performance of such tax return calculations, while requiring some understanding of tax law, is an accounting exercise that does not constitute a privileged communication. See *United States* v. *Davis*, 636 F.2d 1028, 1043 & fn. 17 (5th Cir.), cert. denied, 454 U.S. 862 (1981); *United States* v. *Gurtner*, 474 F.2d 297, 299 (9th Cir. 1973); *Canaday* v. *United States*, 354 F.2d 849, 857 (8th Cir. 1966). Non-privileged communications do not become privileged merely because they are made to or by an attorney. As the courts have consistently held in rejecting petitioners' claim, if a taxpayer who uses an attorney to perform an accounting service were allowed to shield his communications in this manner, the result would be to create an improper "accountant-client" privilege that would be available only to attorneys. *United States* v. *Lawless*, 709 F.2d 485, 487 (7th Cir. 1983); *United States* v. *Bornstein*, 977 F.2d 112, 116-117 (4th Cir. 1992); *In re Grand Jury Investigation*, 842 F.2d 1223, 1224-1225 (11th Cir. 1987).

For these same reasons, documents prepared in connection with tax return preparation are not encompassed within the work-product doctrine. Such documents represent accountant's work-product, not attorney's work-product, even if some legal analysis is inescapably reflected in the financial calculations. As the court of appeals stated, "the documents in issue do not, so far as we are able to determine, relate to [legal] representation" (Pet. App. 9a). That factual determination is not clearly erroneous and does not warrant further review.

c. Petitioners err in contending (Pet. 10-14) that the decision in this case conflicts with the decisions in *United States* v. *Adlman*, 134 F.3d 1194 (2d Cir. 1998), *United States* v. *Abrahams*, 905 F.2d 1276, 1284 (9th Cir. 1990), and *Colton* v. *United States*, 306 F.2d 633, 637 (2d Cir. 1962), cert. denied, 371 U.S. 951 (1963). Those decisions are consistent with the decision of the court of appeals in this case.

In *Adlman*, the court of appeals held that the work-product doctrine may be invoked only with respect to documents that "were prepared 'because of' existing or expected litigation." 134 F.3d at 1198. The court remanded in that case for the district court to determine whether the contested document "would have been prepared irrespective of the expected litigation with the IRS." *Id.* at 1204. In the present case, by contrast, the court of appeals correctly concluded that the draft returns and worksheets were intended "for use in connection with the preparation of tax returns" (Pet. App. 8a) and would thus have been prepared irrespective of any expected or subsequent litigation (*id.* at 8a-9a). The fact that these documents were prepared for this additional, *independent* purpose is what makes them "dual purpose" documents and explains

why they are not protected by any privilege. See *United States* v. *Adlman*, 134 F.3d at 1204 (the privilege is inapplicable if "substantially the same" document would have been prepared for the non-privileged purpose).

Petitioners incorrectly assert that the Ninth Circuit broadly ruled in *United States* v. *Abrahams*, 905 F.2d at 1284, that all communications between a taxpayer and an attorney who prepares a tax return are privileged. Instead, the court held in *Abrahams* only that a taxpayer may attempt to establish that the information disclosed to his lawyer was, in fact, made for the purpose of obtaining legal advice rather than preparing the return. *Ibid.* In the present case, as in *Abrahams*, the taxpayers were given that opportunity but failed to meet their burden of proof. Pet. App. 7a-9a; see 905 F.2d at 1284. As the court stated in *Abrahams*, the burden of establishing the existence of the privilege rests on the taxpayer and there is no "presumptive application of the attorney-client privilege in these circumstances." *Id.* at 1283.

Nor does *Colton* v. *United States*, 306 F.2d at 640, support petitioners' broad proposition. In that case, the court of appeals held that an attorney cannot invoke the work-product doctrine unless the "papers involved were collected or prepared in anticipation of litigation." *Ibid.* In *Colton*, the court rejected the same "blanket" assertion made by petitioners in this case that every communication between a taxpayer and an attorney who prepares the taxpayer's return is privileged. *Ibid.*

2. a. Contrary to petitioners' contention (Pet. 15-20), the court of appeals correctly held that the work-product doctrine does not apply to documents, numerical and otherwise, prepared in connection with audits of petitioners' tax returns. Documents that address tax

planning or audit issues or that relate to the characterization of a taxpayer's finances for tax reporting purposes are not created because of the prospect of litigation. The mere possibility of future litigation stemming from a tax return or tax audit is not sufficient to invoke the work-product doctrine. *Binks Mfg. Co.* v. *National Presto Indus., Inc.*, 709 F.2d 1109, 1119 (7th Cir. 1983). Instead, the "motivating purpose behind the creation of a document * * * must be to aid in possible future litigation." *Ibid.* Petitioners failed to establish that the contested documents were created because of the prospect of litigation rather than to facilitate or ensure compliance with their tax reporting obligations. Pet. App. 9a. See also *United States* v. *El Paso Co.*, 682 F.2d 530, 543 (5th Cir. 1982), cert. denied, 466 U.S. 944 (1984). Because petitioners failed to meet their required burden of establishing that the documents related to legal representation rather than tax return preparation, the court of appeals correctly denied petitioners' claim of work-product protection.

b. The court of appeals also correctly held that petitioners failed to establish that documents created in connection with audits of their tax returns were protected by the attorney-client privilege. As the court stated, "[w]hen a revenue agent is merely verifying the accuracy of a return, often with the assistance of the taxpayer's accountant, this is accountants' work and it remains such even if the person rendering the assistance is a lawyer rather than an accountant. Throwing the cloak of privilege over this type of audit-related work of the taxpayer's representative would create an accountant's privilege usable only by lawyers." Pet. App. 9a. The court explained that, although the attorney-client privilege may attach to documents created in connection with a lawyer's interpretation of

statutory or case law, documents prepared in connection with an agent's verification of the accuracy of a return are not privileged because "this is accountants' work and it remains such even if the person rendering the assistance is a lawyer rather than an accountant." *Ibid.*

This holding is consistent with the established principle that the attorney-client privilege protects only communications made in confidence by the client in the course of seeking legal advice from a lawyer acting as a lawyer. See *United States* v. *Lawless*, 709 F.2d at 487. There is no "accountant-client" privilege. *Couch* v. *United States*, 409 U.S. at 335. Petitioners failed to demonstrate that the contested documents were created by Frederick while he was providing services other than accounting services.

3. Finally, petitioners err in asserting (Pet. 20-22) that the court of appeals applied an incorrect standard of review. According to petitioners, the court of appeals should have applied a *de novo* standard of review in applying the law to the facts of this case (Pet. 22). The question whether the contested documents are privileged, however, is primarily a factual one. As the court stated, "[w]hether a particular document is privileged is a fact-specific and case-specific issue." Pet. App. 3a. The proper application of an evidentiary privilege does not readily lend itself to the formulation of a general rule; instead, it "requires a judgment based on the idiosyncratic facts of a particular case." *Williams* v. *Commissioner*, 1 F.3d 502, 505 (7th Cir. 1993). As the court stated in *United States* v. *Abrahams*, 905 F.2d at 1282 "rulings on essentially factual matters underlying claims of privilege are reviewable for clear error." See also *United States* v. *Laurins*, 857 F.2d 529, 541 (9th Cir. 1988), ("rulings on the scope of

the privilege involve mixed questions of law and fact and are reviewable *de novo*, unless the scope of the privilege is clear and the decision made by the district court is essentially factual; in that case only clear error justifies reversal"), cert. denied, 492 U.S. 906 (1989). Further review of such findings "concurred in by two lower courts" (*Rogers* v. *Lodge*, 458 U.S. 613, 623 (1982)) is, in any event, not warranted. See *Tiffany Fine Arts, Inc.* v. *United States*, 469 U.S. 310, 317-318 n.5 (1985).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

SETH P. WAXMAN
Solicitor General

LORETTA C. ARGRETT
Assistant Attorney General

FRANK P. CIHLAR
ANNETTE M. WIETECHA
Attorneys

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